

ADVISORY

Beyond purchasing

Next steps for the procurement profession

KPMG INTERNATIONAL





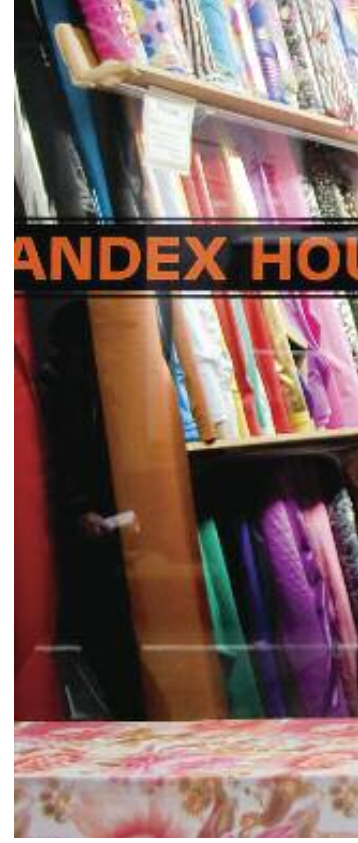
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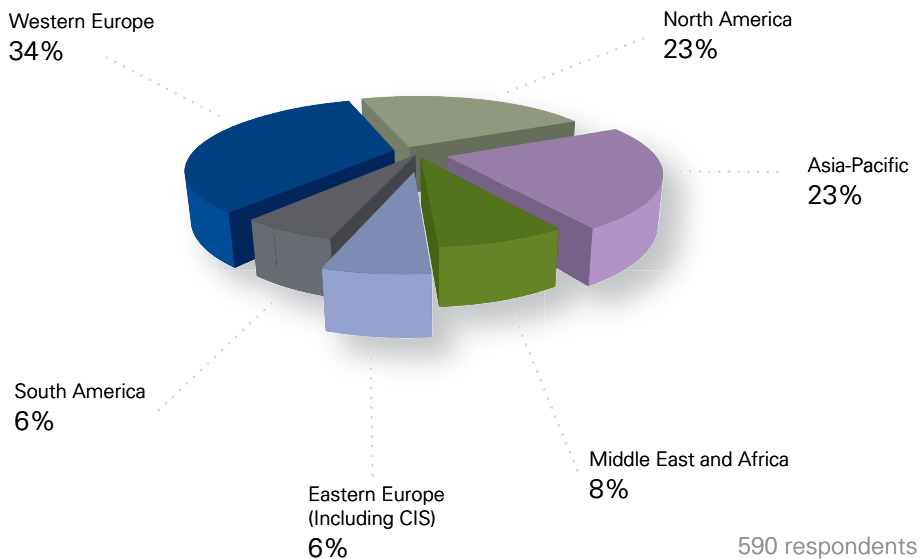
About the research

KPMG International commissioned the Economist Intelligence Unit to write *Beyond purchasing: Next steps for the procurement profession*. The report is based on the following research activities:

- The Economist Intelligence Unit conducted a global survey of almost 600 senior executives. Nine out of ten of those executives have a direct influence on procurement decisions in their companies, while the rest were executives who used the procurement function's services.
- Fifty percent of respondents were procurement or supply chain professionals, but the survey also included a range of other decision makers including CEOs, CFOs and COOs.
- The survey reached a cross-section of industries. Over half (58 percent) of companies surveyed had annual revenues of over \$1 billion.
- All the content in this report was written by the Economist Intelligence Unit, with the exception of the Foreword, KPMG comment and KPMG final thoughts sections.



Demographics of the research



With the exception of the Foreword, KPMG comment and KPMG final thoughts sections, the views and opinions expressed herein are those of the Economist Intelligence Unit and the entities surveyed and do not necessarily represent the views and opinions of KPMG International or KPMG member firms.

The information contained is of a general nature and is not intended to address the circumstances of any particular individual or entity.

All graphs in this report are sourced from research conducted by the Economist Intelligence Unit, 2008. Due to rounding, graph totals may not equal 100 percent.



To supplement the survey, the Economist Intelligence Unit conducted a program of interviews with Chief Procurement Officers and other experts in the field. We are grateful to the following participants for their valuable time and insights:

Jeff Gallant

Vice President, Procurement,
Bell Canada

Paul Snow

Vice President, Procurement,
High Liner Foods

Peter Connelly

Chief Procurement Officer,
Leggett & Platt

Basil Byrne

Director of Procurement Services,
Asia-Pacific,
Nokia Siemens Networks

Dominique Gardy

Chief Procurement Officer,
Shell International

Sui Guan Ng

Vice President,
Commercial Supplies,
Singapore Airlines

Mark Pedlingham

Executive Director of Markets,
Suppliers, and Skills,
United Kingdom Office of
Government Commerce

Professor Richard Lamming

Director,
University of Southampton,
School of Management

Stephen Biesenbach

Chief Procurement Officer,
Vattenfall

Marielle Beyer

Category Team Leader,
External Professional Services,
Zurich Financial

Foreword

Procurement as a function is on a long-term journey toward greater influence. Once seen as little more than purchasing clerks, who could at best leverage the volume of goods required by the organization as a whole to reduce costs, the department's expertise is of growing importance.

At KPMG International, we believe that procurement has the opportunity to become an important strategic player in organizations. It will achieve this by aligning itself with business priorities, and making its planning, sourcing, and vendor coordination central to the creation of value and savings in contracts.

This greater influence will also be found beyond procurement's strategic impact. In an increasingly competitive market, dedicated purchasing experts are essential to cost reduction; bringing to bear not just awareness of current prices, but knowledge of historical trends, alternative acquisition and payment methods, as well as the relevant legal, compliance, and due diligence requirements. Recent recalls

of toys in America over safety concerns shows that effective procurement involves more expertise than simply buying at the lowest price.

To address these developments, and to find out how leading-edge businesses are structuring their procurement systems, KPMG International commissioned the Economist Intelligence Unit (EIU) to conduct research on procurement in the global marketplace. The EIU studied how organizations are currently viewing procurement, and how they see it evolving in the future.

The research shows that organizations understand that they cannot operate without reference to the markets into which they sell: this is also true of the

markets from which they purchase their inputs. Procurement is the part of the business most exposed to the latter and therefore a potentially important source of information not apparent to other executives on opportunities, innovation, competitor behavior, best practice, and certain risk issues. The function is also the point of contact with suppliers, and there is recognition that good relationships with suppliers can greatly enhance competitiveness.

In my years as an enterprise-wide performance improvement advisor, I have come to believe that the biggest issue for the procurement function is to determine how far it can take these strengths for the benefit of the organization.



Beyond these specific concerns, procurement, like the rest of the organization, faces a range of challenges, from the use of IT to sustainability, which will help define its future and what it can deliver to the business as a whole.

We hope this report will provide you with insights into a function that is too often ignored, or just taken for granted, by corporate leadership teams. For organizations willing to rethink this aspect of their business, major competitive advantages can be achieved.

I encourage you to examine your organization's management of procurement, and the opportunities it can offer. I hope that you will find

this research report interesting and insightful.

If you are interested in discussing in more detail how it can guide your organization, feel free to contact your local KPMG advisor or myself.

A handwritten signature in black ink, reading "J Allt-Graham". The signature is stylized and cursive.

James Allt-Graham
jalltgraham@kpmg.com.au

Executive summary

“An army marches on its stomach,” Napoleon famously said. Similarly, an organization cannot survive without its supply chain. Procurement has always had a central role to corporate success, whether simply keeping costs down or even finding scarce commodities essential for operation.

In recent years, however, the function has begun to grow beyond its role as a purchasing agent and realize its proper role in the optimization and management of the supply chain. As competitive pressures have led to the exploitation of ever more complex global supply chains, the importance of expertise within the procurement function has increased. More importantly, the advocates of procurement contend that it can further competitive advantage, especially through strategic insights arising from a knowledge of supplier markets.

This study looks at the state of this key function today, as well as the challenges it faces in adding greater value to the company.

Among the key findings are:

Procurement will win a seat at the strategy table only when it can demonstrate its value to the wider business. Over half of procurement professionals surveyed consider the biggest barrier to their increased contribution to corporate strategy a lack of interest by others in what they have to offer. Those outside the field, on the other hand, are more likely to see the function as too focused on costs and compliance instead of value and innovation.

To play a greater role, procurement needs not only support from the corporate suite, but also to engage in expectation management with colleagues in other departments.

Procurement functions are gaining increasing control over corporate purchasing, and are growing more centralized. In the next three years, the number of businesses where central procurement functions are in charge of day to day purchasing decisions will rise from 45 percent to 54 percent, and the proportion of spend controlled by procurement professionals will rise from a half to two-thirds.

Although the relative merits of centralized and dispersed control over purchasing have long been debated, technological and market changes are making the former best practice.

Large technology investments risk being underused, especially because of inadequate skills. Procurement functions are investing in a wide range of technological tools, from reverse auctions to SRM software, to help in their mission.

Unfortunately these technology deployments often fail to deliver on initial expectations. For example, despite half of companies surveyed having e-procurement tools, only 12 percent of spend is made this way. Worse still, 41 percent of companies do not provide procurement staff with sufficient training to make best use of technological tools.

To make the best use of its investment in IT, procurement will have to focus on training and skills development in this area.



Taxation often needs attention.

Although roughly half of companies acknowledge important tax and compliance implications from global sourcing, only a third have been able to structure their procurement in a tax effective manner. This is surprising, as action here, in the words of Basil Byrne, Director of Procurement Services, Asia-Pacific for Nokia Siemens Networks, “is a relatively painless win.”

Procurement is trying to figure out what sustainability means. Many companies are trying to integrate environmental and human rights issues into procurement — with 42 percent regularly reviewing supplier environmental and human rights performance.

In order to go beyond mere box-ticking, however, firms are having to grapple with just what this means in different contexts, and ask questions such as how much these issues should figure on supplier scorecards. Those who do so, however, have an excellent opportunity to integrate procurement into a growing part of corporate strategy.

Procurement functions and issues at Asia-Pacific companies have a lower profile than elsewhere. In our survey, Asia-Pacific respondents indicated that CPOs and procurement professionals were much less likely to have authority over purchasing strategy and tactics, let alone an enhanced strategic role at the company. Moreover, these companies were less likely to be adopting almost

every popular procurement initiative and a range of software tools.

Treatment of the function as, in the words of one interviewee, a “low-level task” may result from the regional business environment. Unlike elsewhere in the world, Asia-Pacific companies are looking to increase spending and the number of suppliers is expected to increase. Ng Sui Guan, Vice President, Commercial Supplies at Singapore Airlines, however, notes that the function is “becoming more and more important as organizations face rising cost scenarios.”

Section I. A strategic role?

Executives, whether in procurement or not, certainly consider the function important. Among those surveyed, 30 percent give it a very high priority, and a further 44 percent a high one. As procurement centralizes and takes over a greater proportion of purchasing, however, what wider profile will it have in the company?

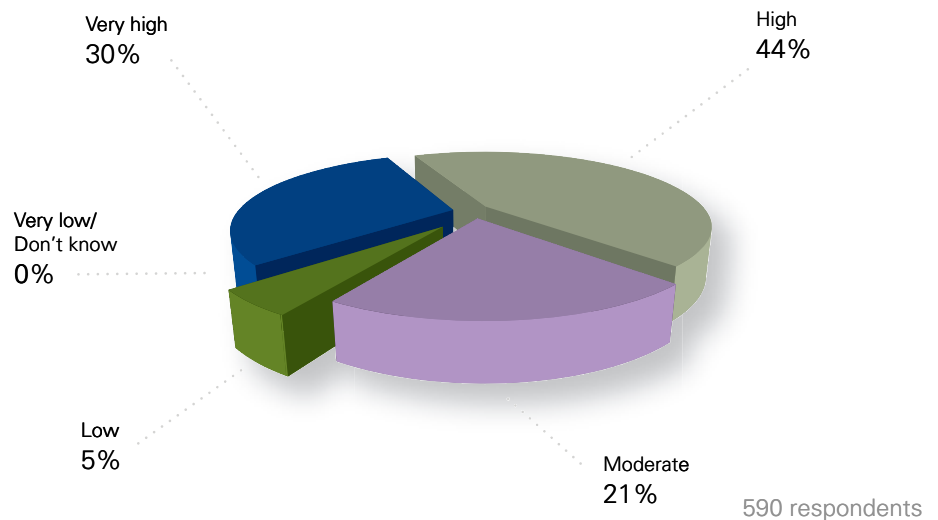
Movement beyond its core responsibility toward a more strategic role is, in some cases, almost inevitable. Paul Snow, Vice President, Procurement of High Liner Foods, a Canada-based seafood business, explains that his company is “still hunting a wild resource (the fish they prepare and sell). Just because it was available two months ago, does not mean it is now. We need to keep the rest of the company informed. It is dependent on what my group can go out and procure.”

In other contexts, procurement can grow into a broader role. One executive working for a large multinational operating in Asia (who wished to remain anonymous), noted that procurement has evolved from just purchasing materials to driving new innovation through products. The company has innovation supply managers who work with key suppliers to come up with product and process improvements.

Despite individual examples, in our survey procurement professionals seem frustrated that their input is not having the strategic impact it could, not least because of the way procurement is perceived by their peers in other parts of the organization.

Those working within the function consider the biggest barriers to

Procurement issues priority





Key findings:

- Three quarters of executives surveyed believe their company treats procurement issues as a high or very high priority.
- Many purchasing professionals believe procurement's role is misunderstood or undervalued, however.
- Procurement has made progress in raising its profile, but needs to do more to gain influence within the top echelons of management.

increasing their influence to be: a lack of interest in, or understanding of, the insight which procurement can offer (cited by 54 percent of respondents); a failure by others to consult procurement on big purchases (44 percent); and traditional resistance to change (41 percent).

More than one in five people within the function also feel that a lack of financial resources leaves them overstretched, and 30 percent do not even think that procurement is a good place for career advancement within their organization.

Mark Pedlingham, Executive Director of Markets, Suppliers, and Skills at the United Kingdom's Office of Government Commerce — its procurement arm — says that although the situation is

changing slowly, rather than seeing the value they can bring, "too many people see procurement professionals as those that keep them out of jail by making sure they comply."

Executive respondents outside the function, however, have markedly different views. Far fewer consider the problems listed above to be leading ones, with only 37 percent citing lack of interest by others, 32 percent a lack of consultation, and 31 percent resistance to change. Moreover, a much smaller number (12 percent) consider the function overstretched.

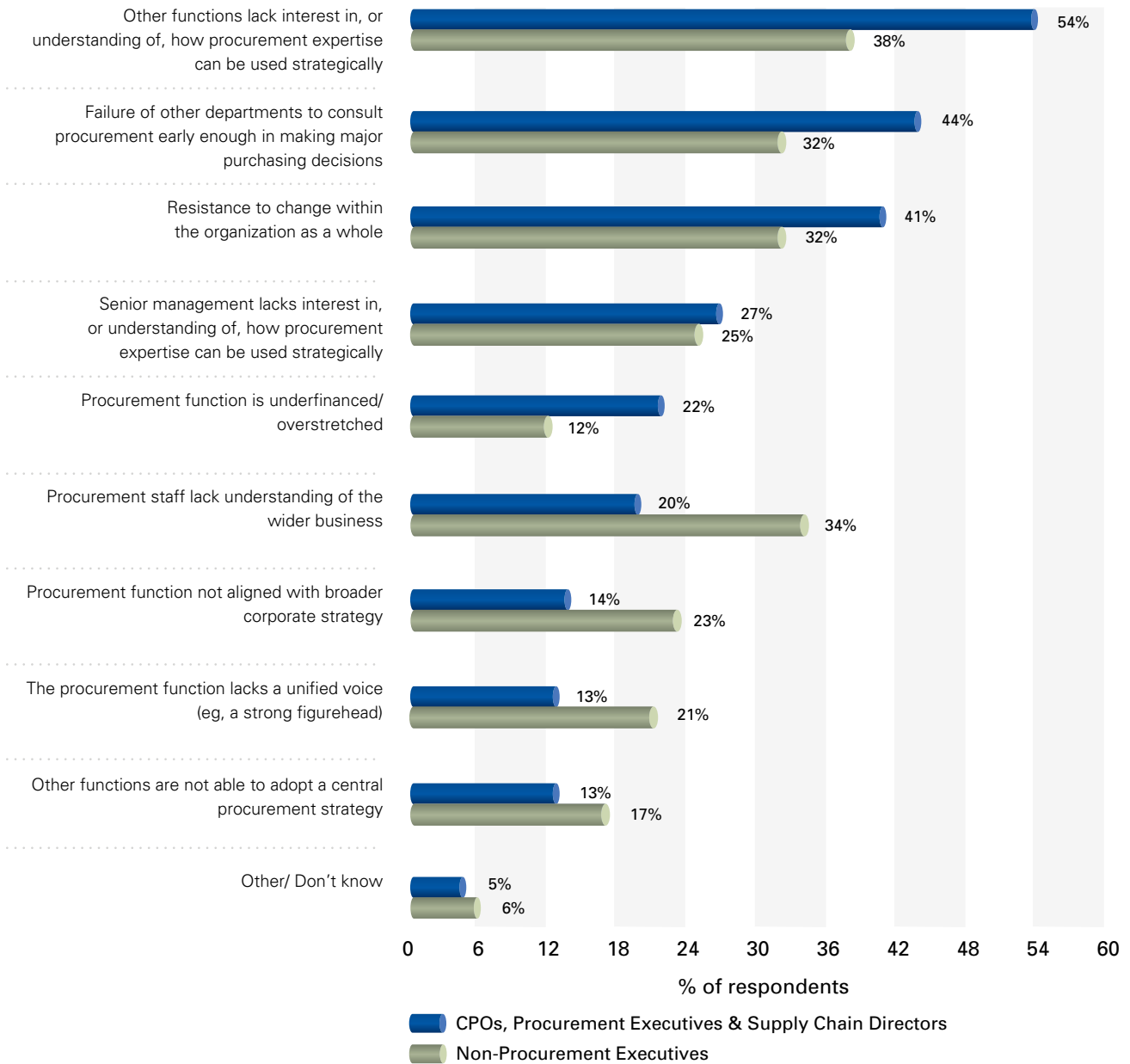
Worse still is disagreement over performance. Among those outside the function, over half (53 percent) think it is too focused on cost at the expense of

value, and 40 percent believe it too focused on compliance at the expense of innovation. Far fewer people within procurement (35 percent and 29 percent respectively) agreed with the previous comparison.

In fact, over a third of those who work for other functions believe that a lack of the understanding by procurement personnel of the rest of the company is a leading barrier to its increased influence, against only a fifth of procurement-based respondents.

This perceptual divide has implications for how useful procurement can be to the wider organization. Two important factors can help procurement to play a greater role. The first is, as with many areas in business, a positive attitude by

The biggest barriers to a greater strategic impact for procurement



the wider corporate leadership. Peter Connelly, Chief Procurement Officer, Leggett & Platt, notes “it has to start at the top of the house. Our CEO and operations guys all support procurement.”

More than attitude is involved. To achieve real influence, the function needs representation within decision-

making. Basil Byrne, Director of Procurement Services, Asia-Pacific for Nokia Siemens Networks, believes that “if we elevate the role of sourcing onto the executive level, you will get a more integrated approach.”

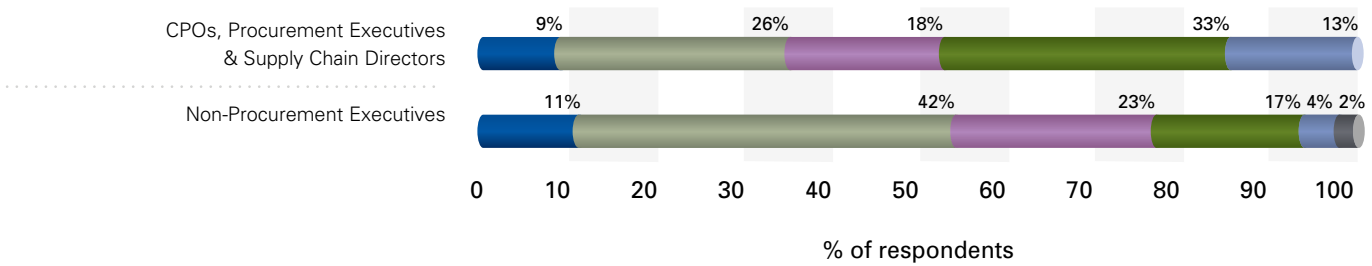
Twenty years ago, there were no CFOs. Accountants were the bookkeepers. Now, accountants have been successful

in developing their profession, and elevating the importance and impact of their role at the executive level. Many CEOs are recruited from CFO positions.

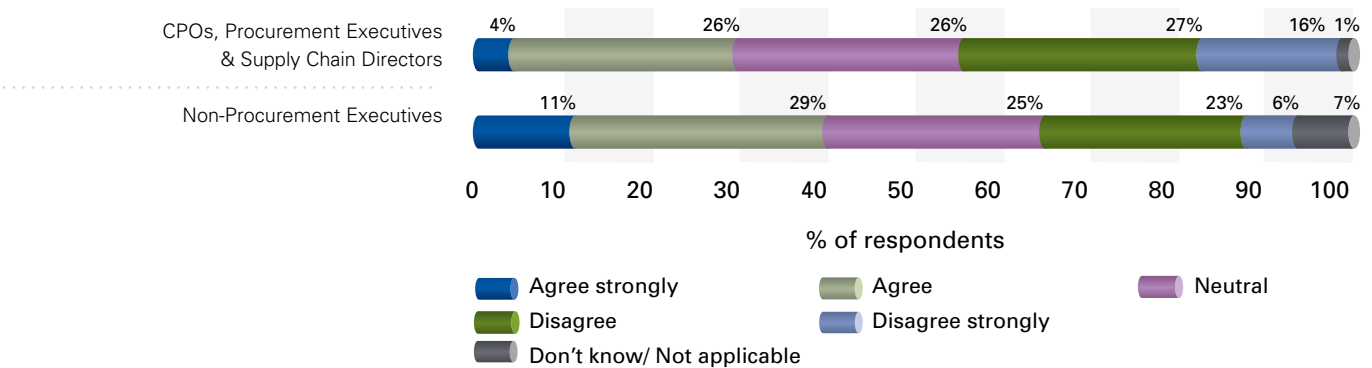
Procurement has a long way to go to elevate the role of the profession and the contribution it can make to businesses at the executive level. “Getting the function to be seen to be

Views on the function

Procurement at our organization focuses too much on simple cost reduction and not enough on value



Procurement at our organization is too focused on compliance and rules-based processes at the expense of delivering innovation in the value chain or business operations



part of the leadership is part of turning it into a valued profession," Pedlingham says. Within the British civil service, five years ago there were very few commercially experienced directors inside operational departments.

"One of big recent changes was to begin to drive level of seniority of procurement folks," adds Pedlingham. "We are still a long way from where we want to be, but there is a growing recognition of the impact procurement can have on departmental budget. The conversation is beginning to be understood."

Just as important as a place at the top table is showing others where procurement might help. A particularly timely specific example is in dealing with

risks arising out of a credit crunch. According to our survey, the most important purchasing-related dangers facing companies by far are supplier continuity risk (listed among the top three by 69 percent of respondents) and commercial risk (64 percent).

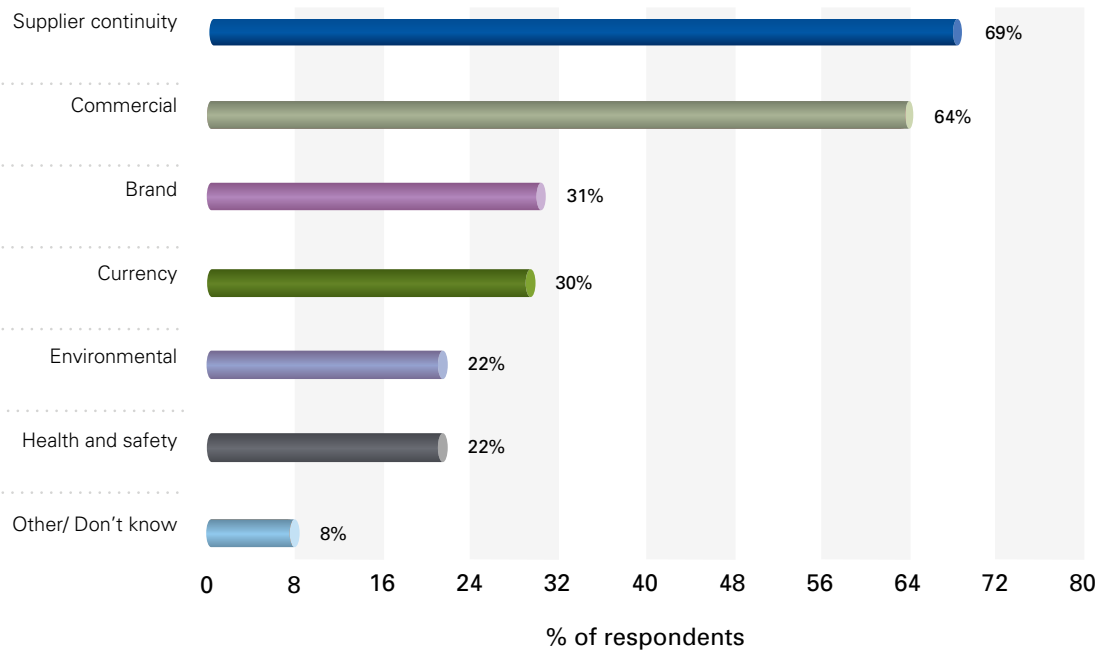
Procurement has the close relationships with suppliers and a strong sense of which suppliers are most likely to suffer credit difficulties. Jeff Gallant, Vice President, Procurement at Bell Canada, sees it as procurement's job "to make sure a supplier is financially healthy," and notes that Bell does regular financial reviews of them. Connelly insists that companies must make sure that they pay not the absolute lowest prices, but ones which allow well-run suppliers to

make a profit. Similarly, Paul Snow, Vice President, Procurement of High Liner Foods, a Canadian-based seafood business, sees altering payment terms to reliable suppliers in temporary difficulties as a risk worth considering.

These are risks and decisions with serious possible strategic consequences for the whole company where procurement's input is key. As Dominique Gardy, Chief Procurement Officer, Shell International explains, addressing such risks is "not a supply chain management affair on its own, but it is one of supply chain management together with the business."

For other functions to understand more broadly where procurement can

Supplier risks



and cannot add value involves overcoming set attitudes.

Marielle Beyer, Category Team Leader, External Professional Services, Zurich Financial, notes “we need to apply our subject matter expertise to add value and better support the business.” Ng Sui Guan, Vice President, Commercial Supplies at Singapore Airlines, agrees: “To work effectively with my business partners, we need to add value to what they are doing. Once they see that value, then procurement can play a more strategic role in helping them achieve their objectives.”

At the same time, others caution that procurement can't be the expert on every product that the company needs to purchase. Byrne explains that “most people in a company think that they've had many years'

experience and that they are really on top of what they are doing. We, though, have hundreds of suppliers with thousands of solutions. There is no simple single answer to how to harness that.”

Jeff Gallant, Vice President, Procurement at Bell Canada, has the opposite challenge. “We have to be careful that the business units don't think we are the absolute experts. Sometimes they expect us to be, and that can cause discontent. We can provide good market intel and research, we just don't have the detailed domain expertise as we are process experts. You have to set expectations properly.”

Professor Richard Lamming, Director, University of Southampton, School of Management, goes slightly further: “I don't think there is a hope of

procurement being seen as advisors on what to buy. Instead, as markets get more difficult, there is going to be a role for somebody who can say 'here is the macro picture', and sometimes to say 'what you want is unavailable and here are alternatives'.”

Once such understanding of where procurement can truly add value spreads through the organization, the benefits — both in terms of strategy and savings — can be striking.





An inside look: Building internal relationships helps everyone at Bell Canada

Programs to cut procurement costs have a reputation in business for falling short of their goals. Reduced spend by professional procurement staff has a way of being offset by expenses elsewhere.

Bell Canada has been going through a major cost-reduction exercise. Jeff Gallant, Vice President Procurement, notes that his function, rather than simply charged with buying, "is a strategic driver across the organization which has the ultimate responsibility of being the change agent in reducing costs." In 2006, procurement saved costs amounting to hundreds of millions of dollars, and its efforts continued in 2007.

To what does Gallant credit procurement's success? He explains that "often companies do a great job of negotiating cost savings with the supply base but cannot materialize it in the organization. To do so, it has to be an

inclusive and collaborative process with other business units."

Such cooperation must take place at different levels. At Bell, for example, the Chief Sourcing Officer is on the Management Board "so he can alert the business unit presidents, the COO, the CFO, and the CEO, to get their buy-in at a high level" on relevant issues including, where needed, choice of supplier, and to provide relevant expertise to them.

"Another key component," says Gallant, "is buy-in at the working level." Here is where Bell's approach is truly innovative: once procurement is ready to implement savings, "we develop a detailed, analytical business case at the business unit level, to determine each units' cost savings." It presents the ongoing results of the cost-reduction efforts monthly to the business unit controllers, who all participate in a Benefits Realization Council.

When a controller signs off on the savings, as happens for about 90 percent of the reductions which procurement identifies, "the budgets

get pulled out, and the business unit is motivated to use the strategy." The procurement team assists further by helping with change management, and analyzing spend at the unit level.

Gallant notes that "once savings materialize, we get good business support." He adds that "implementation and change management at a local level are critical. Financial planning and budget takeout is critical as well to make sure that everyone has the right incentives and is aligned."

To foster strong relations with the business units, procurement has "to set expectations properly." Rather than being an expert in individual areas of the company, the function can provide market intelligence as well as "ask the right questions." Gallant notes that good relationships with internal customers mean that departments which have not worked with procurement in the past are now more willing to do so. The results of such cooperation are invariably better than working alone — for example, his department recently reduced supplier costs for Human Resources by \$3.5 million.

KPMG comment: Procurement must earn its place at the strategic table

The maturity of procurement departments varies enormously across different organizations. In our experience, it is this level of maturity that determines the profile of the function. A procurement team with a strong leader and capable senior people will have an organization that is relevant and central to the business. A team that lacks this leadership will tend to function in isolation and remain removed and largely irrelevant to the business.

Procurement should be working with different units across the main part of the business, and be involved in the strategic planning, sourcing, and lifecycle management of their major spend categories. Many procurement functions remain isolated from the main parts of the business and don't deal with the major input costs of such things as materials. Procurement becomes focused on doing analyses of spends and contracts, and indirect procurement: It fails to work to become integrated with the core business operations across the organization.

Control of spend illuminates procurement's importance

Procurement's importance can be assessed by a simple question: What percentage of the organization's spend does procurement have direct involvement in across the four primary procurement responsibilities—strategic sourcing and planning, source to contract, procure to pay, and end to end management of the procurement process?

Many procurement operations deal only with indirect spend. Large direct spend areas are given to specialist areas. For

this to change, procurement must first work to understand the needs of each business unit, and then customize its focus and expertise. Once it is knowledgeable and trusted, it can take on a greater role.

In the majority of organizations, procurement exists as a separate, centralized function focused on analysis. It ends up trying to impose a system, and then complaining that units are not following policy, and are buying from non-preferred suppliers. These purchases are often a necessary investment by groups and individuals closer to the organization's day to day needs.

Centralized procurement teams must move to a more decentralized or center-led structure, with smaller teams working closely with other business units. With this CLAN, or Center Led Action Network in place, the senior procurement officers take on a more strategic role in a smaller unit. When these senior officers are involved in the process and procurement understands local needs, business units are more willing to support procurement.

The value of strategic procurement is demonstrable

It should be supported, as this model of a center led, strategically based procurement function is proving to be cost effective at global sourcing.

Tax effective, direct procurement structures using hub and spoke global sourcing structures are taking as much as 40-45 percent of total costs out of the operations.

A mature, and integrated procurement function is successfully integrated into an organization's business operations, across all four of the areas of procurement responsibility previously noted. Just as importantly, it works closely with the business to ensure that the third party contracts meet and exceed the clearly defined business requirements. Through this process, the procurement team will be able to track and report on savings which have been baselined, captured, fully realized, and then protected so they are not lost.

Large, centralized procurement teams often struggle to move savings from the captured to the realized stage, due to limited integration with the business. When procurement creates savings, they can disappear if they are not protected from being spent on other things. This is done by working with P&L officers at budgeting times, and focusing on reducing where and how departments spend money.

Procurement can add its greatest value to an organization by becoming an important partner at the senior most levels. For the arguments about responsibility and influence to become irrelevant, procurement must make itself relevant to every possible part of the business. Procurement must change the perspective that management may have of it by realizing its potential, and maximizing the value of the skills and capabilities the procurement team may possess.

Written by KPMG

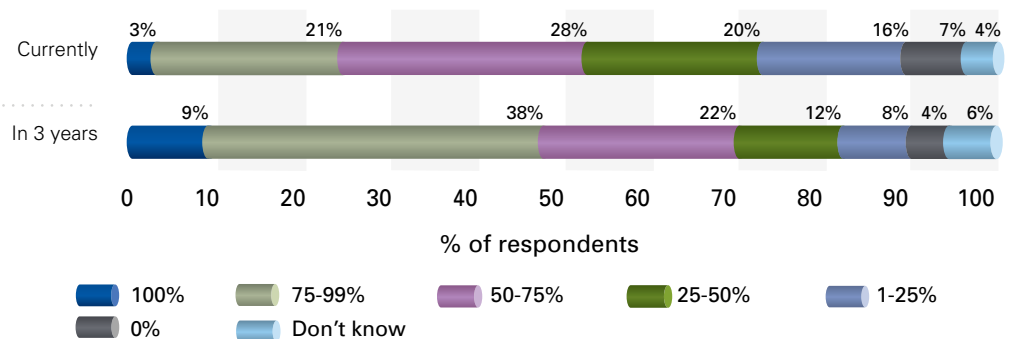
Section II. Procurement functions and purchasing: Growing control and centralization

Procurement increasingly holds the purse strings in many organizations today, consolidating control over its central area of concern. Our survey indicates that a growing proportion of corporate spend is falling under the control of procurement professionals and departments.

For example:

- Over half of companies report significant reductions in maverick spending over the last three years, against just 18 percent which have had less success.
- The percentage of spend controlled by procurement professionals looks set to rise from a half today to two-thirds in the next three years.
- The proportion of companies where people outside the function, such as business line managers, make ongoing purchasing decisions will drop from 19 percent to 10 percent in the same time period.

Total procurement spend (direct and indirect) which is negotiated or contracted by procurement professionals, today and in three years





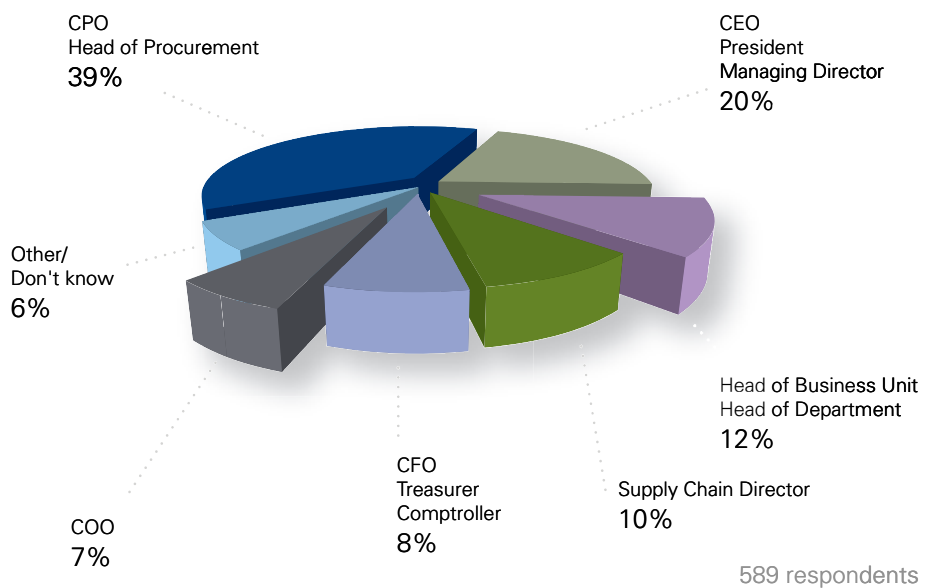
Key findings:

- Procurement will continue to gain greater control over global purchasing over the next three years.
- Most firms will favor a centralized approach to purchasing as a way to increase their leverage with suppliers.
- CPOs are taking a lead on procurement strategy in half of the companies surveyed.

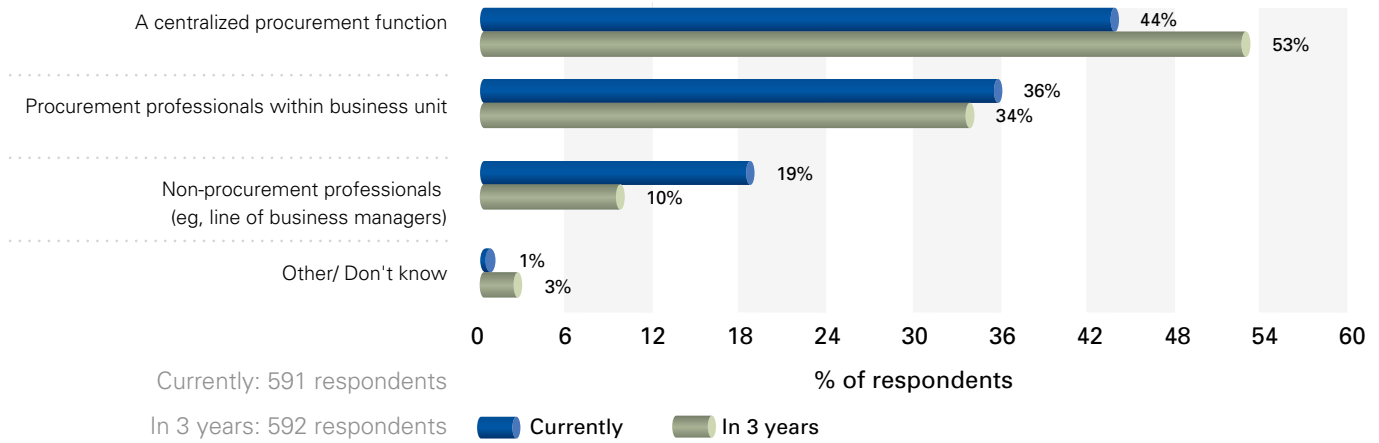
- CPOs and Supply Chain Directors have the primary responsibility for procurement strategy at 49 percent of companies, with CPOs twice as likely as CEOs to have that role.

The shift toward professional oversight of procurement strategy and its day-to-day implementation may even accelerate the degree of spend under procurement's control. Among survey respondents who work within the function, procurement is involved with controlling the spend and providing direction of roughly two-thirds of overall purchasing, and appears poised to rise to 85 percent over the next three years.

Primary responsibility for setting procurement strategy



Primary responsibility for day-to-day decisions on procurement today and in three years?



As procurement gains a greater influence over buying, it also is expected to centralize, with respondents indicating that the proportion of companies where a central function is in charge of day-to-day purchasing will go from 45 percent to 53 percent in the next three years.

Although the exact numbers vary somewhat by region and company size in all of these areas, the broad trends are the same across the board.

The debate over the relative merits of centralized and dispersed procurement is an old one. Professor Richard Lamming, Director of the University of Southampton’s School of Management and an authority on procurement, says “it is a pendulum. You can argue either side cogently, both theoretically and practically.” At the moment, technology, macro-economics, and “obvious candidates for centralization in the light of world markets and world prices” are driving opinion in one direction. That said, other interesting possibilities, like the federal principle — doing certain procurement centrally at a group level, and other procurement where

appropriate in a dispersed way — remain relatively untried.

Centralization does not necessarily mean a uniform structure. In some cases it means moving procurement up from a national to a regional, rather than worldwide, level. Shell, the global energy company, has yet another approach. Dominique Gardy, Chief Procurement Officer, Shell, prefers to speak of globalization rather than centralization. “I think it is a balance between two forces: proximity to the business, which is very key to adding value, and globalization to ensure that we standardize as much as we can all across the businesses. I cannot see an organization where all of this will be in one location.” Gardy’s company’s efforts in this area therefore seek “to lever the size of the group as much as we can, but still execute where the business is.”

Whatever the specifics, the direction of travel is certainly toward some centrally controlled arrangement. Peter Connelly, Chief Procurement Officer, Leggett & Platt, a diversified manufacturing company that has seen significant

financial and other gains from centralizing procurement (see Case Study: Leggett & Platt), says “every other company we talked to had gone to a centralized model. It is now best practice.” Stephen Biesenbach, Chief Procurement Officer of Vattenfall, the Sweden-based power company, is also convinced that, for his company, “centralization is better.”

In addition to the obvious gains from leveraging the volume of purchases across the firm, he notes two other large benefits. First, a centralized function helps provide greater transparency throughout the company, avoiding problems such as where “we had one supplier that was blacklisted in one country and a strategic partner in another.” Second, it helps with the effective implementation of strategy. Standardization, for example, has to be “more than saying it would be nice if you could standardize a bit,” and then being ignored. A central function can push these initiatives far better.



An inside look: The benefits of centralizing procurement at Leggett & Platt

A perennial debate within procurement revolves around the benefits of centralizing decision-making against those of devolving responsibility. Our survey indicates that advocates of the former currently have the upper hand. What are the benefits of such an approach?

Leggett & Platt, headquartered in Carthage, Missouri, is a Fortune 500 company that manufactures a diverse range of engineered components and products worldwide. Its 28 business units, with 280 independent facilities, operate in 20 different countries.

Until recently, each facility made independent procurement decisions. By the end of 2008, however, a centralized function of 20 directors will do all of it. Connelly, Leggett & Platt's Chief Procurement Officer, reports that the company has spent \$6 million in procurement enterprise investment and within three years realized \$5 million in benefits.

The most obvious advantage of centralization has always been leveraging the buying power of large purchases, and Leggett & Platt is no exception: as Connelly says, previously "we were buying eggs by the one, not by the dozen." He notes that when the company started combining orders several years ago from five or six facilities, instead of leaving the purchasing to individual plants, "everywhere we did it we found 10-15 percent savings. We knew there were savings out there."

The benefits, however, went further. A big difficulty of the previous system was trying to coordinate 280 decision-makers: "it was like herding cats." This is now much easier.

Moreover, purchasing personnel did not always have the scope and expertise to do the job as well as they should. The new system makes training in areas like IT usage much more viable. Connelly notes "you can't train 280 users; there are competency issues. We are now down to 20." It is now easier to train this core procurement team to use strategic tools. In particular, the smaller number of procurement directors has let the company introduce an enterprise-wide purchasing system which lets it track prices and vendor quality.

The people no longer involved in purchasing after the changes have been redeployed successfully into product planning, value engineering, and supply tasks across the business units.

"We think there are millions in savings as purchasing people get assigned to other responsibilities. It will release our resources."

Finally, streamlining the purchasing system is letting the function play a much more strategic role at Leggett & Platt. Furthermore, "When we had 280 chiefs around, we were too busy with transactions. It is a time issue if you are doing 5,000 orders at \$1,000 an order. By centralizing, we'll reduce the orders. It will release the handful of experts" to help with strategy.

There have been many benefits following centralization, but the transition was not easy. Connelly has seen "a lot of human push-back. We have been decentralized for 125 years, and have had one acquisition every month for the last ten years. Change is difficult when people are running their own show." Nevertheless, support from the top has been key to driving through change. "The CEO and COO are squarely behind this and could not be more supportive. With the money involved, it's a no-brainer."



Written by KPMG



KPMG comment: Globalization adds new options to an old debate

While the debate over centralized versus a dispersed procurement function is certainly an old pendulum, globalization has created a new option: center led procurement. A Center Led Action Network, or CLAN, has a core of activity in the center, with a greater or lesser amount of resources dispersed; located near the operations. The center consists of senior procurement experts developing strategy, risk guidelines, and categories of spend. Mid and lower level staff can be physically located as seems best.

CLAN structured procurement will, of course, need to vary from organization to organization. It is, however, becoming the structure of choice for global businesses that understand the linkage between procurement and supply chain management, and want to profit from that understanding.

We are fascinated to observe that the center led model actually creates larger savings than the traditional centralized model. This may be because a centralized function is less in tune with the needs of the business units on the ground. Center led procurement is intrinsically more in touch with local knowledge and practice. By being both at the strategic center while still out in the trenches, it has a better ear for the entirety of the business.

Center led procurement offers all the strategic advantages of centralized procurement, including better control resulting in more cost savings. But the less obvious advantages are of getting consistency in approach and the approved ability to prioritize key issues, combined with a better ability to make big decisions. Center led gives procurement a sense of strategic goals and of being about more than just cost reduction and compliance: it can provide more efficient management of the organization's working capital which must be the true goal of good sourcing.

Center-led procurement breaks down internal barriers

We are also noting subtle advantages in personnel issues. Centralized procurement sometimes exists as a silo in the organization, making it difficult to move people in and out and creating a potential dead end in the company: there is little motivation for the best and the brightest to go into it. In a center led structure, other staff work closer with the junior procurement members, and the senior team is at the strategic table. This turns procurement into a more attractive career path, and silences the traditional criticism that procurement doesn't understand what we do.

While center led procurement is not as straight forward to manage as the other models, it does drive better behaviors and, in our experience, is worth the extra effort because it tends to achieve higher, more sustainable, savings.

The system is best determined by the strategic goals

To reorganize for the most effective procurement structure, a business must first ask why they are doing it, and determine clear goals based on targets and benchmarks. In our experience, organizations need to be clear whether the move is being made to reduce supply costs or internal costs, and base their decisions on strategic goals, not just business school models. The function's plan also needs to have buy in from the relevant senior people. The speed of the move should be determined on a case to case basis. Enormous cost pressures may force a business to move more quickly, but it should not be at the expense of developing clear strategies and goals before acting.

The final determinant for the best procurement structure is always this: Does it make it easy for suppliers to give you their best offer?

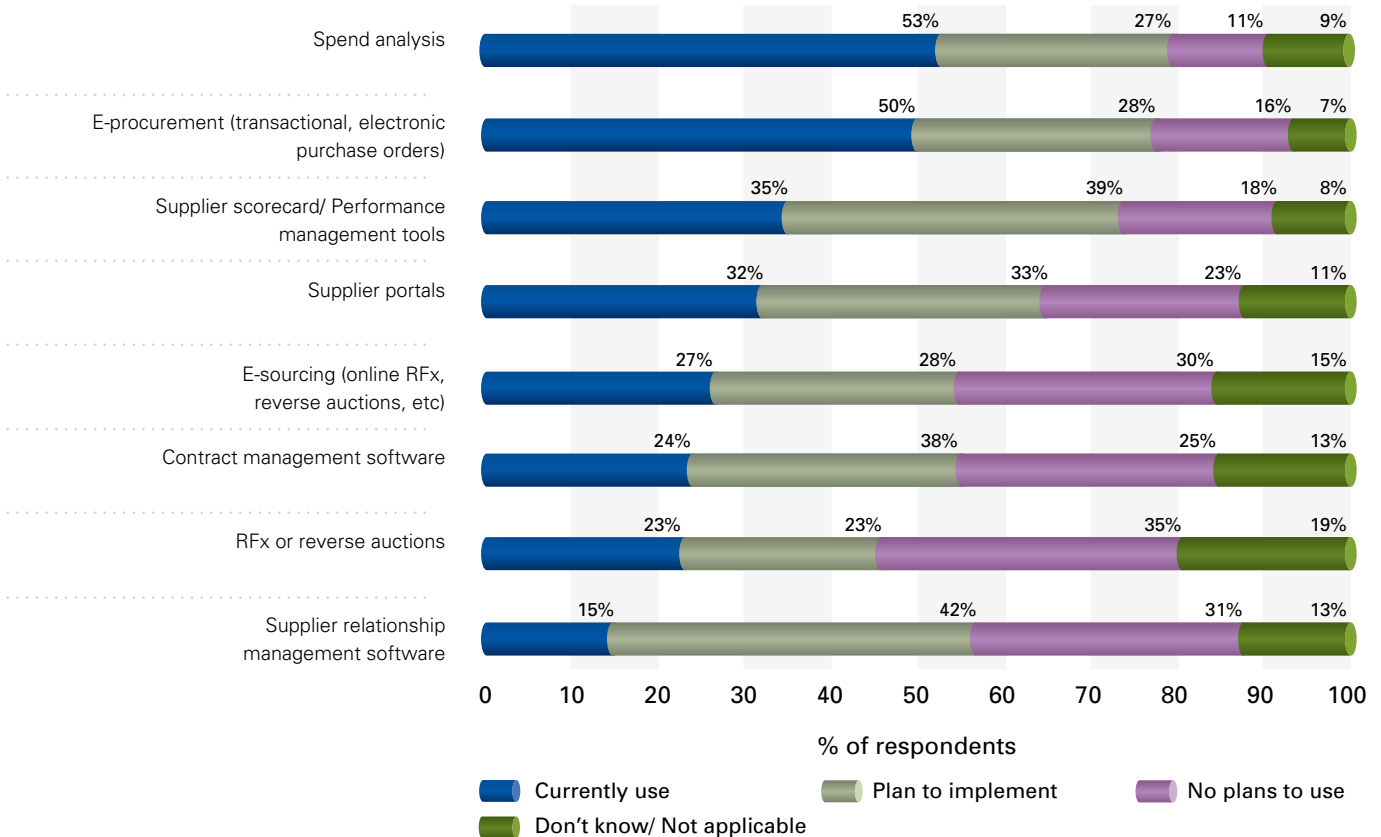
Written by KPMG

Section III. Information technology: The need for smarter investment and training

Executives and experts interviewed for this study agree that improved use of information technology is essential for procurement: Shell’s Dominique Gardy cites it as critical in such a rapidly changing world. Professor Richard Lamming, Director at University of Southampton’s School of Management adds, “when the dust settles on the rhetoric about a flat world, there is still a profound challenge for people in procurement to use technology in a competitive way.”

Companies in our survey are certainly acquiring such capacity. Half already use spend analysis and e-procurement software, and in each case nearly 30 percent more intend to implement these within the next three years.

IT tools used, today and in the near future



Key findings:

- IT tools for procurement are becoming more popular, with half of companies already using spend analysis and e-procurement software.
- Although investment in IT is increasing, training is required to enable procurement staff to make full use of these tools.
- Companies should improve ease of use of these tools not just for employees, but also for suppliers.

For a range of other IT tools — supplier portals, e-sourcing, RFx or reverse auctions, contract management software, and supplier performance management tools — between about a quarter and a third of those surveyed currently use them, and the numbers in each category are set to more than double in three years. Supplier relationship management software, now in use at only 15 percent of companies, should be present at more than half within the same time period. In short, the typical company will have most or all of these tools in place in the very near future.

Having the capacity, however, does not mean being able to use it. For example, Mark Pedlingham, Executive Director of Markets, Suppliers, and

Skills, United Kingdom Office of Government Commerce, notes that “e-procurement hasn’t had the full traction we expected five to seven years ago.”

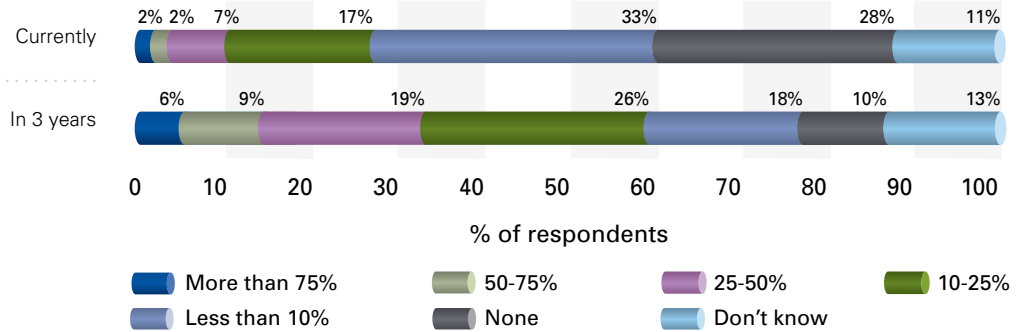
Despite the widespread presence of such software, on average our survey indicates that only 12 percent of total spend is sourced in this way. More alarming, at 41 percent of companies, procurement staff are not trained to make full use of IT tools: only 27 percent say they provide such education. Lamming goes further. “People in procurement have been sidetracked by the minutiae.” In particular, he believes companies need to adapt technology to their strategic needs, but worries that “I don’t think that many of them are ready for that.”

Various roadblocks exist to greater success in using IT in which so many companies are now investing.

First, the basics matter. Procurement IT can only work where the technology as a whole can function. Especially in the rapidly developing economies of Asia, bandwidth constraints and multiple different national Enterprise Resource Planning platforms within a broader company are often today’s reality. Pedlingham adds that attitudes are important in this regard too: even in modern European offices not everyone trusts computers.

Second, software has to address procurement requirements as they exist. Bell’s Gallant explains regarding e-procurement that “companies gravitate

How much spend is channeled through e-sourcing or e-procurement (e-RFx, e-auctions), today and in three years



initially toward electronic catalogues.” However, only 10 percent of company spend is capable of being fit into these at the moment, so Bell has started to implement new service categories, such as contract labor.

Marielle Beyer, Category Team Leader, External Professional Services, Zurich Financial, faces similar challenges when working with professional services, where a definition of “services” is often less tangible and difficult to define: “It is obviously easier to create a catalogue for tangible goods like office supplies. For professional services, there are limitations with catalogue orders.”

Going beyond e-procurement, Basil Byrne, Director of Procurement Services, Asia-Pacific for Nokia Siemens Networks, notes that “we have tools for tenders, quotes, and electronic auctions that we use in a fairly limited way. A lot of the services we buy are quite complicated, and we need to price them in a complicated way because our customers want it that way. To turn that into electronic RFQs requires considerable effort” and the result is not necessarily repeatable.

In considering process requirements, companies also need to remember that procurement is a function which involves those outside the company as well as internal employees. Singapore Airlines now has an extensive e-procurement program: evaluation and selection of proposals are largely conducted online, and, upon appointment, suppliers and the company transact electronically via EDI for purchase orders and invoices. Sui Guan Ng, Vice President, Commercial Supplies, Singapore Airlines, recalls, however, that “one of the early challenges was really the acceptance of suppliers. They were more used to submitting hard copies of proposals or having face-to-face meetings.

As more and more organizations embraced technology for their procurement, suppliers were forced to adopt the e-procurement technology as a prerequisite for them to do business with us. They realized that e-procurement is not a zero sum game; both parties benefit from it in terms of extended customer/supplier reach and cost effectiveness in back-room processing.”

Finally, the technology must be used in such a way that its adoption does not obscure the search for true value. Gardy explains that Shell was an early adopter of many IT tools in this field. “The e-tools very often relate to price. Price may be important, but the total life cycle is even more important.” They are less useful when trying to work together with suppliers to find the best value proposition for all concerned. He concludes that “engagement with suppliers at an early stage can be far more effective. E-procurement is more relevant to areas where price is the critical lever.”

Whatever the difficulties, IT is something procurement must get right. Pedlingham observes that “those who have invested in these tools have a much better understanding of their spend. They are very effective if you have the right processes attached and their value has been fairly demonstrated. If you don’t understand what you spend, how you spend, and with whom, it is hard to manage it.”





An inside look: Making IT fit procurement's needs at High Liner Foods

One way to improve the effectiveness of procurement IT is to make it fit the needs of the company, rather than have the business adapt to the strengths of the technology.

High Liner Foods, one of North America's largest seafood providers, was forced to go global in its search for raw materials (seafood) after the collapse of the Grand Banks fisheries and the subsequent sale of the company's fleet in the 1990s. It soon found that worldwide sourcing was generating excessive paperwork, and challenges in both tracking shipments and informing suppliers of requirements.

The solution was an add-on to the firm's ERP system, which lets everyone in the supply chain, including suppliers, shippers, customs brokers, and the

company have transparent, real-time access to the information they need to do their jobs. They can also update the data directly on the system. The web-based technology has become essential to how the company does business. Says Paul Snow, Vice President, Procurement, High Liner Foods "we don't know how we could operate without it. It has become a tool we need to use."

How the technology was created and introduced is as important as the underlying software:

- Snow believes that "the primary reason it has been successful is that we have an IT group in our company that is interested and dedicated to developing these kinds of solutions." The model was developed internally, although it has also had extensive attention from a third-party software company.

- The software dealt with High Liner's most pressing requirement. "The main part of what this is about is really involving people involved in the transaction, and letting them go in and perform their various functions. The information is visible to everybody, and saves a lot of communications, paper work, and emails."
- It did not try to do everything at once but left room for development. For example, it does not do supplier performance rating. "That's really the next step for us", says Snow.
- It did not reinvent the wheel. By building on its existing ERP platform and working with a long-term software partner, the project minimized the need for new training and accelerated development of the solution.

Written by KPMG

KPMG comment: IT wrestles with the challenge of growing importance

In a corporate environment of global sourcing networks, IT is rapidly becoming king. Global sourcing networks, extended geographies, and the need for more effective structures increase the importance of effective enabling tools. But what KPMG is seeing is a king with some very real problems, and one that is being constantly asked to grow, adapt, and integrate in ways that it is finding difficult to do.

Procurement requires an efficient supply chain, and real savings can be had through the kind of smart global sourcing that a streamlined IT system can provide. However, that improved use of information technology is constantly being challenged by old legacy systems in the supply chain that resist or defy integration.

This problem of integrating legacy systems is exacerbated by the fact that very few people understand the whole supply chain in most organizations. We have found that procurement teams generally don't understand the complexities of a corporate IT system, while its IT specialists rarely totally comprehend procurement. This can result in real confusion and damage done. Most organizations that are wrestling with global integration in procurement are in need of individuals who can grasp this big picture and stay on top of the disparate forces.

Organizations often mistake a business problem for an IT problem

Integration also fails because the team responsible focuses on the IT solution as an end in itself. Businesses that make the move to an IT driven global procurement system most successfully start with the business case. They determine the business outcome they want in 2-3 years time, and then decide which IT system will get them there. They also make structural changes first, and then bring in IT to achieve certain goals.

KPMG member firms are too often asked to apply their expertise after the money has been spent, the system installed, and problems have arisen. This may be an inappropriate, but necessary time to address shortfalls. Disciplines must be in place, and there must be a cultural readiness in the organization to deal with a new system. Training must also be given in how to use the system, and in how to use the information it generates. Few companies are doing this: most tend to overspend on implementation, and then cut back on training to balance a predetermined budget.

When a business fails to implement properly, it can affect the entire supply chain.

They who have the most information win

Businesses that implement global IT systems correctly stand to experience huge benefits. Done right, it gives the organization the ability to control its suppliers, and that is where all true cost savings in procurement come from. The procurement team wins when it has the information and insight to back up its demands for cost reductions from suppliers, and can consequently pass on lowered manufacturing and distribution costs to its customers. Whoever controls the information flow in a procurement chain has to power to control the relationship.

There is, however, a trick to that. Given the power of modern IT systems, we at KPMG are very focused on getting our clients to recognize the difference between information and insight. There is so much information being made available now that our most successful clients are hiring mathematicians to process it. Processed correctly, it is giving them the ability to predict what people will do.

This does require bodies to accomplish, though. The traditional view was that a good information system allowed the user to reduce head counts. In global procurement today the systems are so complicated and far reaching that the data requires an enormous amount of analysis. It has become a specialized field in itself. Specialists are needed to produce the returns and savings that a good IT system will generate.

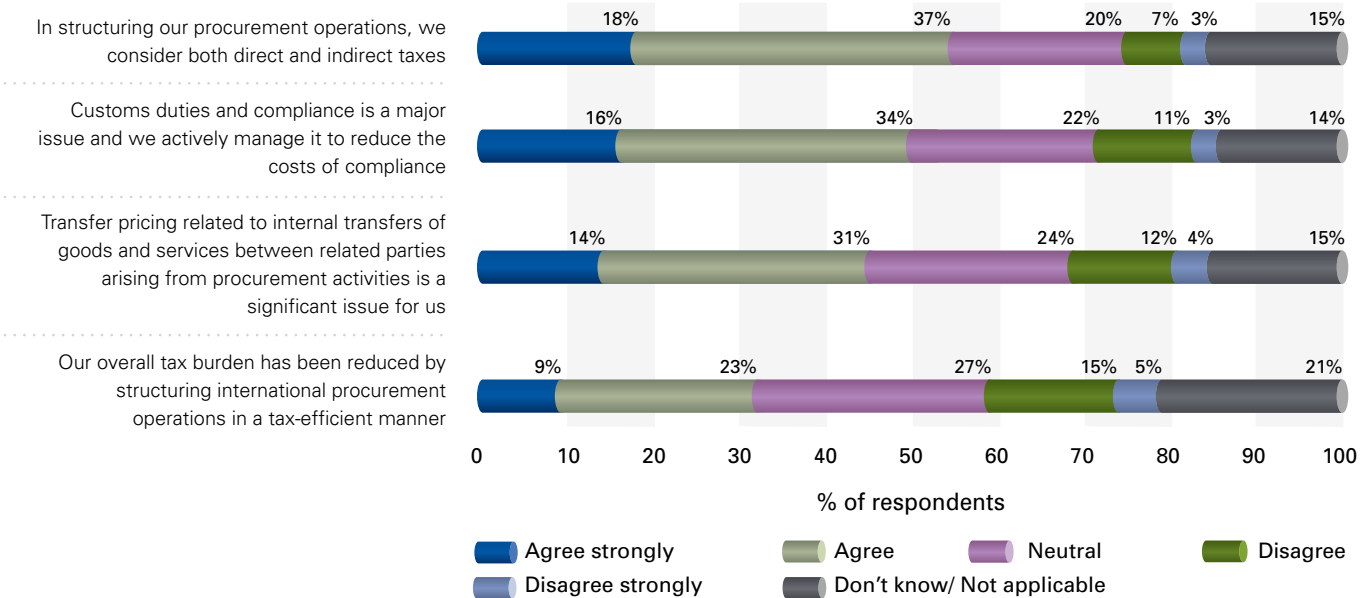
Written by KPMG

Section IV: Taxing challenges

In supply chains that span multiple countries, different corporate and indirect taxes and customs duties can complicate the lives of procurement professionals: many recognize the problem, but fewer have been able to address it successfully.

To an extent, tax-related difficulties, and options for dealing with them, are industry, or even company specific. Paul Snow, Vice President, Procurement, High Liner Foods, for example, explains that High Liner is “guided very little by duties or taxes: we are confined by where the product can be found and a lot of the materials are not subject to duty.” Similarly, Stephen Biesenbach, Chief Procurement Officer, Vattenfall, notes that “to be honest, we don’t feel that this is really an issue for us.” With large and strategic suppliers, Vattenfall can usually arrange for delivery to its national businesses by a supplier subsidiary in the same jurisdiction.

Views on international procurement operations





Key findings:

- Although tax concerns vary by company, half of respondents see customs duties as a major issue for procurement.
- Tax barriers are a serious consideration when planning procurement strategy.
- However, only one in three respondents has been successful in reducing the tax burden on purchasing.

Such companies, however, are in the minority. In our survey, half agree that customs duties and compliance are major issues which they actively manage, against 14 percent which do not. Even more (55 percent) structure their procurement operations to take account of direct and indirect taxes, and 45 percent find that tax issues complicate internal company transfer pricing. One Asia-based executive interviewed noted that, "Tax is the biggest barrier for the free movement of goods. A duty of 10 percent kills regional sourcing."

It is therefore surprising that in the survey only a third of respondents report success in reducing their overall tax burden by structuring their

international procurement activities in a tax-efficient manner. Moreover, just 9 percent say that they have implemented tax-efficient procurement structures, although a further 18 percent are currently doing so and 26 percent are considering them. A broader, executive-level understanding of tax-related opportunities associated with procurement would likely stimulate more interest in these types of initiatives.

Simply comparing how many respondents consider this a major issue and how few have had success in the area shows that a notable number of companies have room to improve here. The gains can be dramatic. Connelly estimates that

roughly "30 percent of the benefit of going offshore is in tax/currency considerations. It is hugely important to us." He also recalls that a previous company for which he worked saved \$40 million a year simply by procurement structuring its purchases in a tax-efficient manner. Byrne adds another advantage of focusing here: "in many ways, it is the easiest thing to do because it is a relatively painless win. It does not hurt your suppliers."



KPMG comment: Viewing procurement from a tax perspective

This survey raises a fair question to ask: If so many businesses recognize that by structuring their procurement function smartly they can reduce their tax burden, why are so few doing it successfully?

Our conclusion is that businesses tend to fall into two camps: those who view taxes as a controllable cost, and those who view them as an inevitable cost they can't do much about. The reality is that any business that has a procurement division with a global sourcing mandate should be looking at its supply chain from a tax perspective. They need to look at the feasibility of restructuring, and get a sense of the benefits they will experience from a reconfigured procurement function. Then they can move to set up procurement in a tax efficient location.

Tax and procurement: It's time to start talking

To successfully do this requires a close interplay between the tax and procurement departments. The profile of tax departments varies hugely across businesses, with no real pattern, but we see fairly consistently that procurement is usually not tax aware. So this function is often managed and determined without considering the tax implications. And while it has not been usual for these two divisions to work closely together, any business that wants to compete globally will be at a disadvantage if it does not pay attention to this potential saving. The quickest ways to get goods to market may not actually be the cheapest. For example,

a European business that purchases goods manufactured and assembled in China may in fact save money by paying less duty if it has the goods partially assembled in the EU.

Any globally functioning business must look at customs, duty, specific national taxes such as VAT, and corporate tax in determining the most profitable way of bringing goods to market. This is part of the new reality that businesses are scrambling to keep up with.

The exact specifics of how to best take advantage of this depend on the industry and the business. However, one of the advantages of a center led, as opposed to a centralized procurement team is that the senior management and strategic leaders don't have to move. The people who do the actual procurement can either be relocated to a low tax area, or others can be hired there. The only requirement is that the contracts are initiated and registered in the low tax location.

Global businesses need to consider global tax implications

Companies are becoming more tax aware, especially when reorganizing. Procurement functions should be judged post tax, and included in the savings. Most business taxes tend to be ignored and profits tend to be looked at pretax. If procurement was responsible for paying customs duty, they might look more carefully at the tax implications of their purchasing decisions because when procurement is made more tax efficient, the result is a more profitable business. This way, procurement adds value to the organization and becomes a strategic function.

By placing it in a low tax region, the business is able to keep the profits there. Of course, they must also consider that a simple low tax area might not be the best option. They can set up procurement in an area that has losses, and use these losses against procurement costs. It's all a new way of thinking, and a product of globalization.



Written by KPMG

Section V. It's not easy being green

Almost everyone interviewed for this study noted that sustainability — in particular its environmental aspects — was a rapidly growing concern for procurement. Paul Snow, Vice President, Procurement, High Liner Foods, notes that “two years ago sustainability wasn’t on the top of our radar list. It is much more important today.”

Not only are consumers expecting it, a seafood company obviously must ensure a sustainable supply of its products. Dominique Gardy, Chief Procurement Officer Shell International, adds that such considerations are “critical, especially in certain parts of the world.”

Our survey shows that sustainability is starting to have an impact:

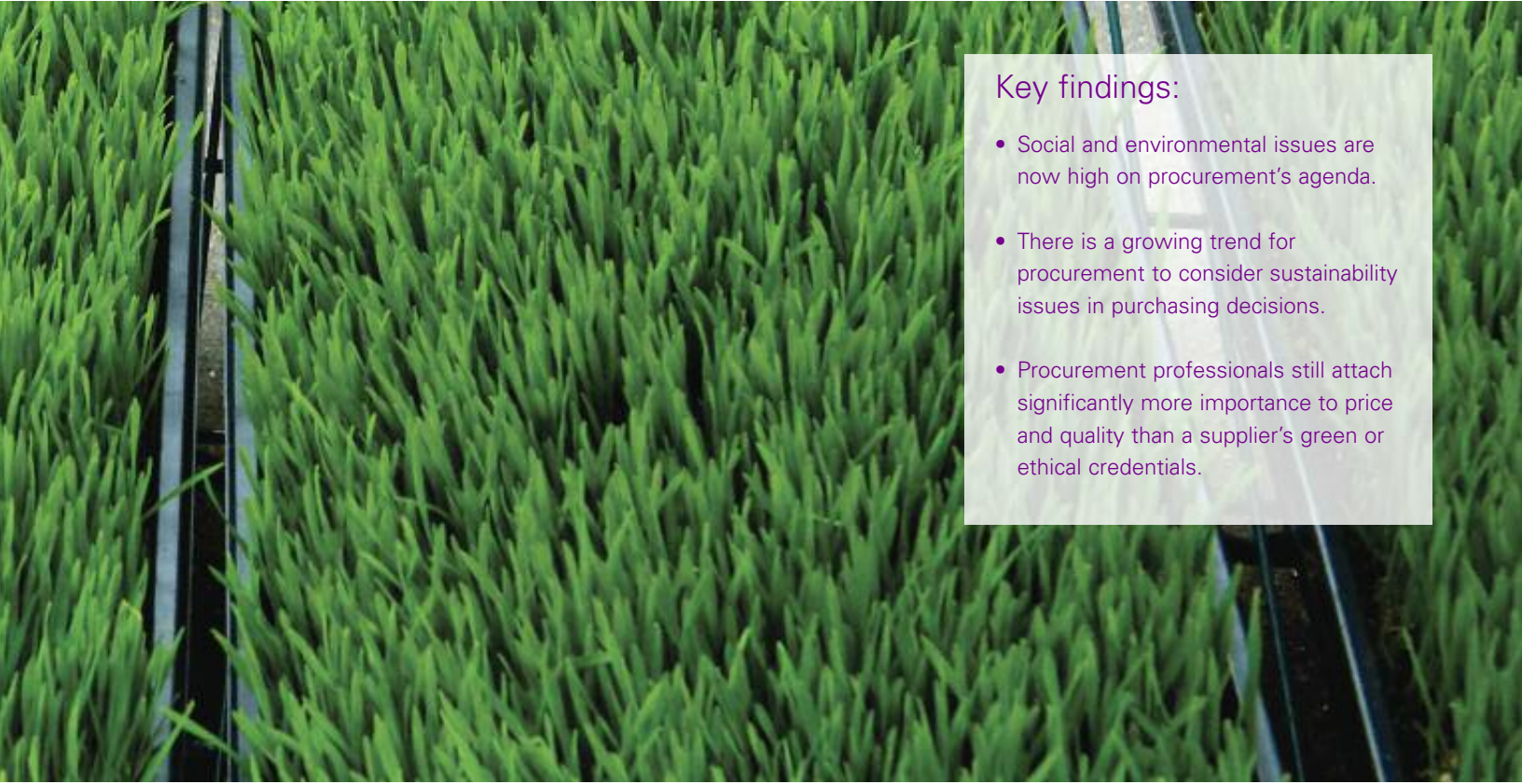
- 43 percent of organizations have started, or are working on, introducing social, ethical, and human rights considerations into procurement decisions. Another 28 percent are considering doing so.
- 33 percent have begun, or are in the processes of starting to, reduce the environmental impact of products by working with suppliers. In this case, a further 31 percent are considering doing so.
- 42 percent regularly evaluate suppliers on environmental and human rights performance.

The broader impact of such change in practice is less clear. When presented with a list of ten supplier attributes, those surveyed considered — predictably and understandably — quality, price, and reliability as by far the most important. The environmental and social records of suppliers, however, figured last, with just under a third of companies considering them more than moderately important, as against 93 percent, 88 percent, and 82 percent for the three leading issues.

One reason for the low import given to environmental and social concerns may be that some procurement functions use certain sustainability criteria as initial filters rather than giving them a significant weight in supplier

scorecards. Basil Byrne, Director of Procurement Services, Asia-Pacific for Nokia Siemens Networks, “before we engage any supplier, we put them through a detailed assessment process, including asking a wide range of questions about all aspects of their business, site visits and assessments or interviews. We’re quite confident that this process would show up any human rights issues. That would be a go-or-no-go hurdle for us.” Thus, in some cases sustainability criteria may not seem to factor into deciding the winner, even though they had already done so by defining the playing field.

In not doing more here, procurement is missing a valuable chance to align itself with corporate strategy. There



Key findings:

- Social and environmental issues are now high on procurement's agenda.
- There is a growing trend for procurement to consider sustainability issues in purchasing decisions.
- Procurement professionals still attach significantly more importance to price and quality than a supplier's green or ethical credentials.

are potential cost benefits to increased attention to sustainability, in particular from purchasing products which require fewer environmental inputs, such as energy.

More importantly, Professor Richard Lamming, Director, University of Southampton, School of Management adds that "there is a great deal of money to be made by showing consumers that you are interested in saving the world. Procurement being the guardians of a clean bill of health for products is going to be critical to its success. It really has a role to play in making the company look good in terms of provenance of goods and services." Finally, at the level of

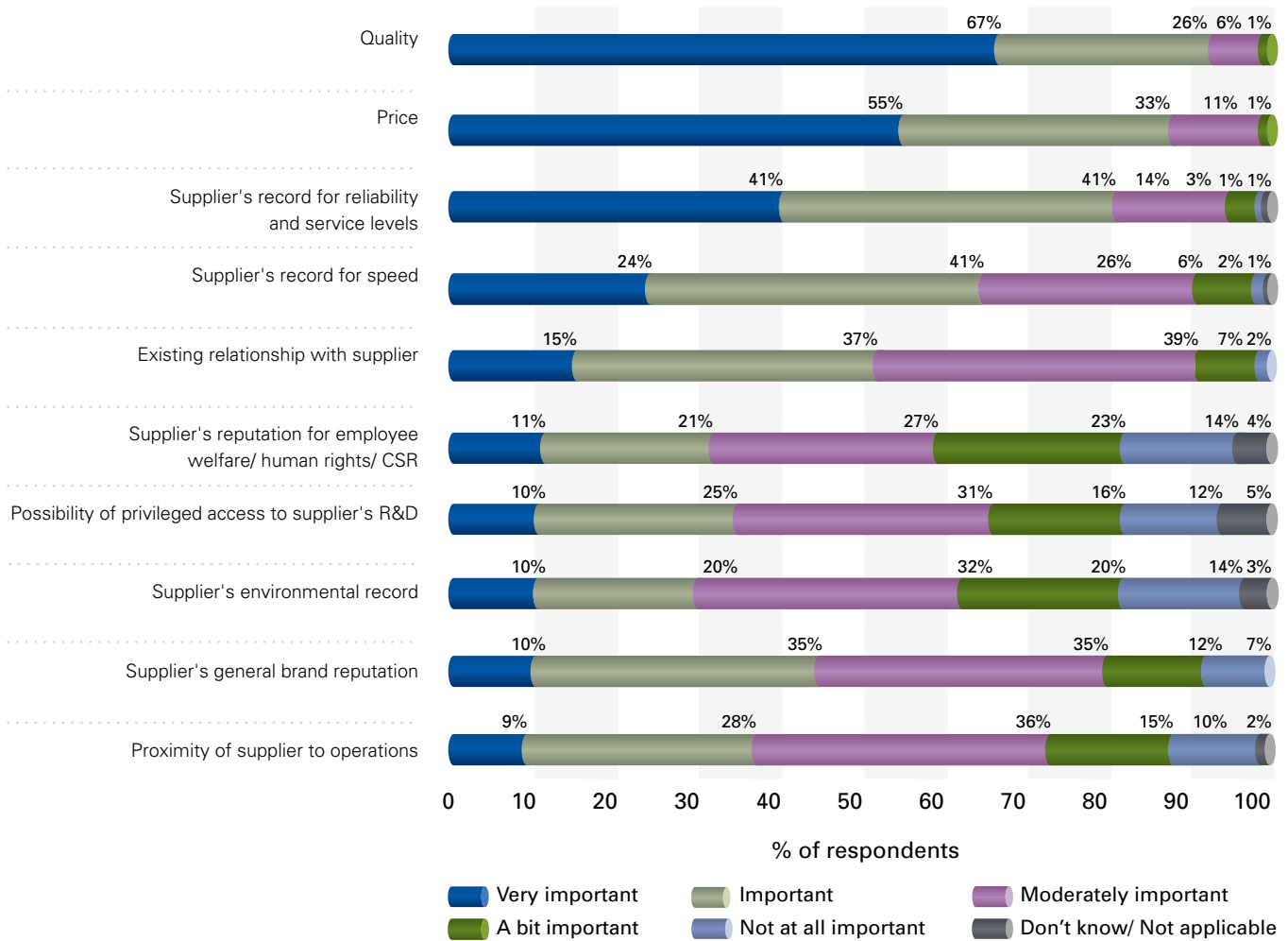
overarching corporate strategy, as Biesenbach says of Vattenfall, "when we have a CEO going around worldwide encouraging people what to do when it comes to climate, we have to find a way to transfer that strategy to our procurement activities. By doing so we are closing the gap between our corporate aspirations and procurement actions."

What exactly this means for procurement is something many leading companies are still working out. For Biesenbach, the questions at Vattenfall include: "if we are aware that a supplier is struggling [in these areas], will we kick him out? In such a case, if there are only one or two suppliers,

what does it mean to us? Also, it is not just about asking people 'yes or no', we have to learn how to evaluate what they are telling us and we have to be open to investing in activities to ensure that suppliers are fulfilling our requirements and committing to our strategic ambition to be number one for the environment."

Shell has much longer experience in this area. For Dominique Gardy, Chief Procurement Officer, Shell International, "supply chain management has a key role to play in support of business delivery" with issues such as safety, greenhouse gas emission, and local content of purchases all having an important part. He finds that focusing

Importance when selecting a supplier for a major contract



on the life-cycle costs of assets, instead of only upfront costs, helps greatly in this regard. Consideration of broader organizational goals can also help. In government, for example, Mark Pedlingham, Executive Director of Markets, Suppliers, and Skills at the United Kingdom's Office of Government Commerce, notes, "you can look at the boundary you draw around procurement. If you look narrowly you

may end up with one particular answer. If one of your government policies is around local employment though, you might consider that it was more cost effective to use local labor because the cost of delivering that employment would be higher another way."

As Gardy says, "in many cases it is not necessarily easy, but that is not an excuse not to address it," especially as

procurement's contribution to corporate sustainability looks set to become an increasingly important part of its performance and an area where it can make a marked contribution to corporate strategy.



An inside look: Zurich Financial — What you are buying matters

Procurement is no monolith: the purchase of different types of inputs requires a variety of strategies and processes. More important for this study, the nature of what is being sourced has a fundamental impact on the challenges facing the function in the years ahead.

Marielle Beyer, Category Team Leader, External Professional Services at Zurich Financial, explains that the very high level of spend involved in her field presents its largest challenge: “[These purchases] attract a lot of attention within the company. Senior executives want to know what the return is.” While it is relatively easy “to identify an owner or key stakeholder for direct goods, professional services may have different business owners across the organization.”

Her experience is not unique. In our survey, more than three-quarters of respondents involved in procurement decisions have a role in the buying of professional services, against about only about half for the purchase of direct, indirect, or capital goods.

“The more practical challenge,” says Beyer, “is that professional services are

not as tangible as a direct good. It is very difficult to put together business requirements on a piece of paper.” This results in several complications. For example, as noted earlier in this study, in using e-procurement or spend management systems, it is harder than with tangible goods to create a catalogue and execute purchases. With professional services “you have to look at non-catalogue purchase orders, because there are always additional elements of complexity.”

The nature of the product also changes how several key issues are approached:

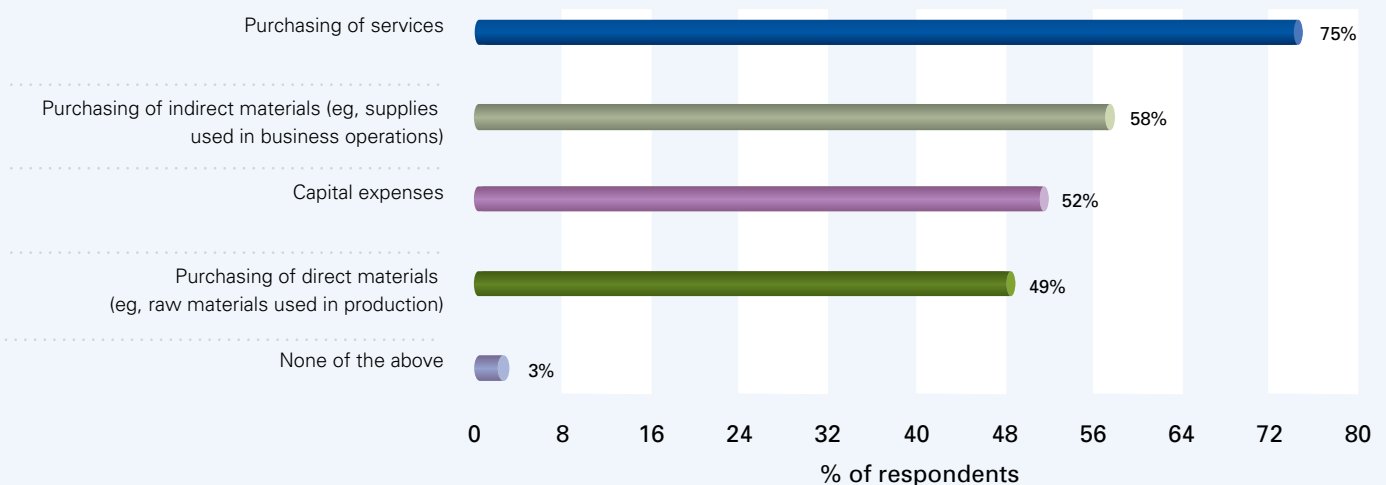
- Risk Management: “Supplier discontinuity is a big risk when purchasing goods,” notes Beyer, “but in professional services that particular risk is relatively low.” Most professional services suppliers are broadly based and are relatively financially stable companies. “Instead, the bigger dangers are from giving work to a vendor that doesn’t know our company very well or may not provide us with the right teams — the B or C teams rather than the A teams.”

- Tax: Here Beyer explains that “any kind of mitigation is on the top of our agenda.” That said, in her area, the “potential is relatively small,” limited largely to shifting the location of the services purchased to mitigate value-added tax. Even here, the possibilities are “diminishing.”

- Sustainability: Zurich Financial has been active in addressing issues such as climate change and sustainability more broadly and the issues are a growing concern for procurement at the company. Beyer notes, though, that “it is generally easier to introduce good governance for the procurement of material goods. In professional services, clearly corporate social responsibility is on the table, but it is a very new topic to us.” A steering committee is currently trying to determine how to evaluate the supplier base in this area.

Of course, professional services procurement also faces problems common to the function as a whole, such as issues of cost, value, and spend management. Understanding how these challenges vary across different areas of procurement, however, will increase success in addressing them.

Respondent influence on procurement decisions



Written by KPMG

KPMG comment: The quest for sustainable business practices affects procurement's approach

As the profile of sustainability rises, every aspect of an organization is being challenged to respond, and procurement is no different. We agree with the findings from this research that leading businesses are still figuring it out but, in our experience, there are some valuable signposts.

A firm bottom line is that businesses must listen very carefully to their customers and their investors. This issue is moving quickly up the list of their concerns. Any business that has a difference in values between itself and its customers puts itself at risk, and any business that does not respond to changing circumstances is in danger of being left behind.

The job of procurement on the question of sustainability, as with most issues, is to align itself with corporate goals and tie actions back to the profit drivers in the business. For example, a mobile phone company would be best advised to pay more immediate attention to the issue of radiation in its phones than to its carbon footprint, while a retailer with trucks and facilities must focus more on lowering its carbon output.

Sustainable procurement begins with supplier selection

Once a connection is drawn to corporate goals, procurement can develop a sourcing strategy that incorporates sustainability. First achieve a basic level of trust with the supplier base. Supply qualification

processes can help to imbed sustainability into the selection process early. The important issue here is that sustainability, like any real metric, must prove itself with performance numbers. Procurement must be able to track and demonstrate its success with data; this cannot just be an exercise in feeling good.

There are no definitive global standards for assessing potential suppliers' greenness. CO2 emissions, water quality, child labour, and recycleability have differing importance for different industries. It can also depend on consumer perceptions as much as realities. For example, buying flowers in Great Britain from growers in Holland would seem to be a more ecologically sound procurement practice than air freighting them in from Kenya. But at least one study has shown that growers in hot houses in Holland produce more CO2 emissions than does air freighting in the equivalent weight of flowers from Africa.

The trade off exists where a business exposes itself to commercial risk. A toy company who uses a price driven supplier that illegally contracts may save money, but when the lead content in the toys proves hazardous, the toy company will be the loser. A business with a global procurement function can use audits on supplier bases and long term relationships to avoid this, but there are no generally accepted answers yet.

Uncertainty over carbon trading and carbon footprints

The most generally acknowledged metric for sustainable business practices is the carbon footprint. The first step for any business is to reduce carbon usage. Aside from sustainability issues, this will also help reduce business costs. In the UK, the Carbon Trust is helping businesses to achieve this. The next step is to offset the rest, but even the more environmentally savvy businesses are standing back from this because it is costly and complicated. The perception is also that there is not enough regulation and clarity in this field yet.

So what are the cost benefits of a sustainable procurement strategy? For consumer facing businesses, the major one is a marketing upside. Businesses that are perceived as living values that are becoming increasingly important can benefit from being viewed positively. Other benefits will vary.

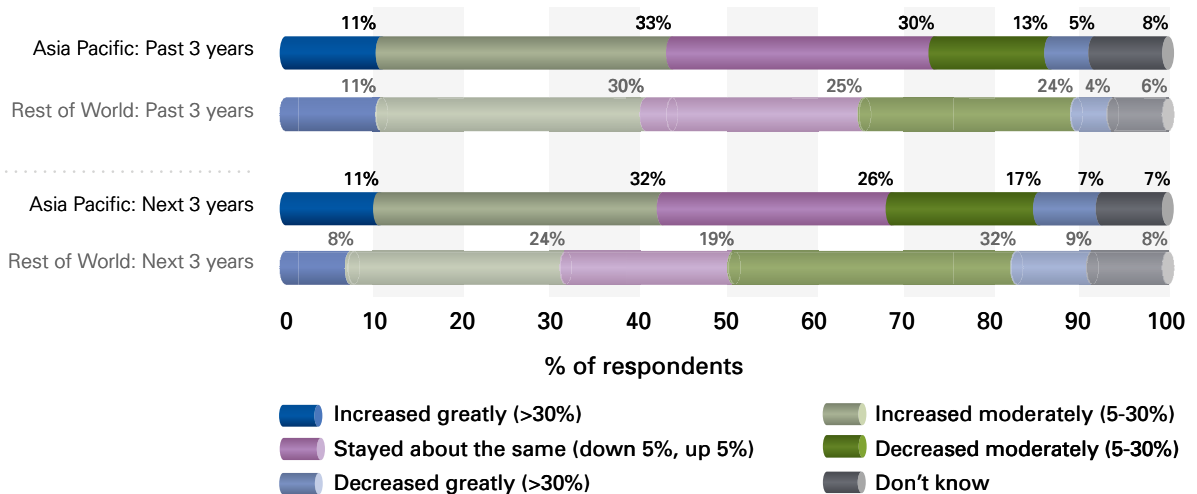
Section VI. Global differences: The procurement function in the Asia-Pacific region

According to our survey, procurement is lagging behind as a function in Asia-Pacific countries:

- Day-to-day purchasing decisions are more often in the hands of non-procurement professionals (for 26 percent of regional respondents) than in the rest of the world (17 percent).
- CPOs are much less likely to have primary responsibility for procurement strategy (24 percent to 42 percent).
- Except for tax-efficient procurement — as noted above a particular concern in the region — companies in the region were less likely to adopt any of a series of popular procurement strategies listed in the survey, and were also less likely to have installed, or to be in the process of installing, any of a variety of advanced IT tools.
- Finally, the problem of procurement personnel not sufficiently understanding the business to have a broader impact within companies was far more widespread, cited at 42 percent of respondents from the region, against 27 percent elsewhere. The war for talent, an issue across the globe, is particularly relevant in this area, especially as companies expand.



Change in number of suppliers to respondent organizations, over the past three years and in the next three years





Key findings:

- Procurement has been a relatively low priority for Asia-Pacific companies, and a professional purchasing function is only beginning to emerge in most companies.
- Talent shortages are making it difficult to find procurement staff who fully understand the business.
- However, a strong procurement function could give companies in the region an extra competitive advantage in a tougher economic climate.

For Basil Byrne, Director of Procurement Services, Asia-Pacific for Nokia Siemens Networks, the description of the Asia Pacific point-of-view rings true. "Most companies treat procurement as a low-level task. It is not treated as strategic. Very few people in this area are aligned with sourcing accreditation agencies. The situation is changing, but still quite slowly." An Asia-based executive felt that procurement was a "relatively young" profession in Asia.

Another reason for procurement's position in the region may also simply be that the demands of the local marketplace differ. Top line growth is a priority in rapidly growing markets, and Professor Richard Lamming, Director, University of Southampton,

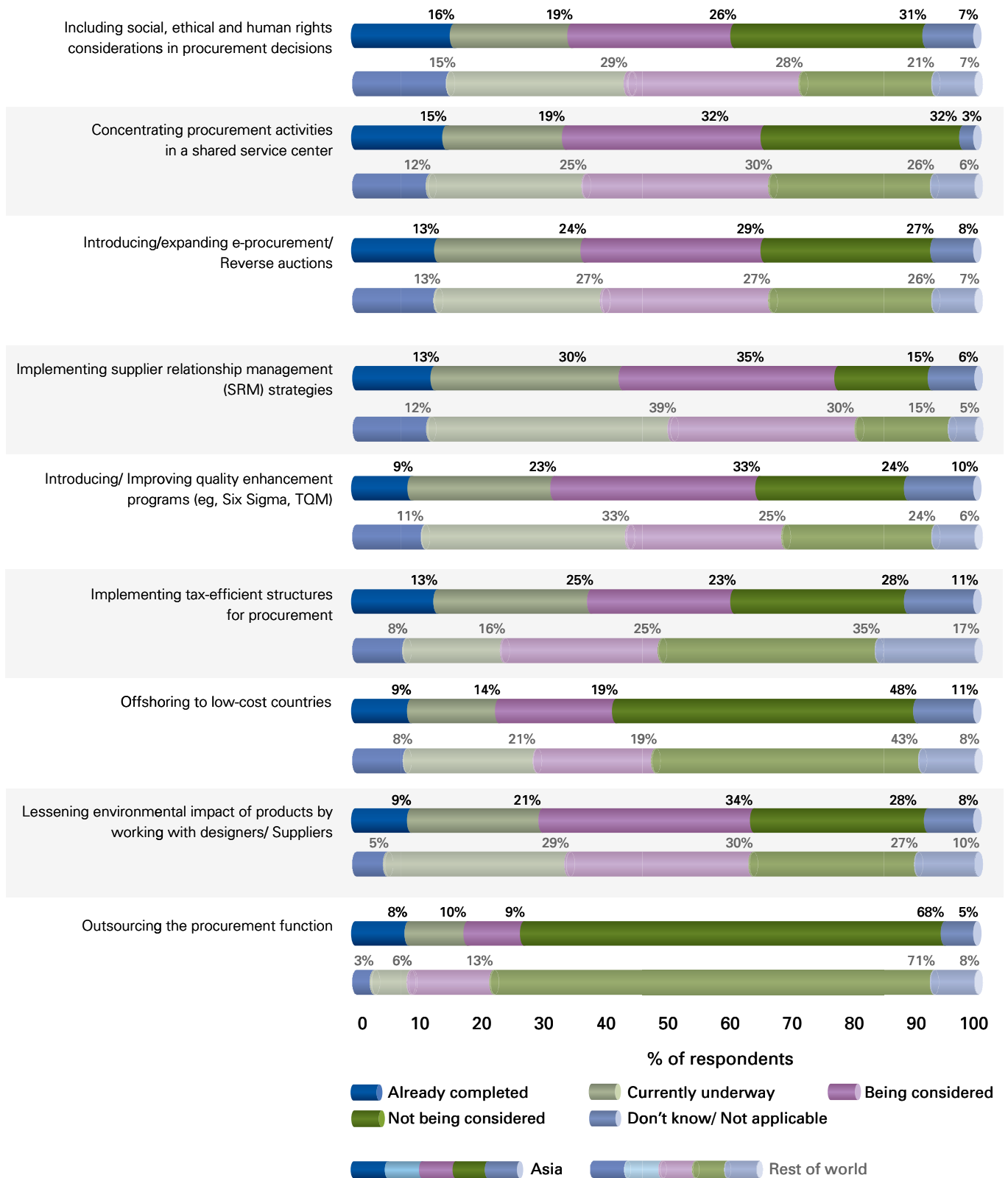
School of Management, thinks it is possible that businesses are not paying attention to procurement because "they are too busy getting on with business." He notes that the situation is similar to that of Japan during the years of its greatest economic growth.

The procurement goals of Asia-Pacific companies certainly suggest that they are more focused on expansion. For example, the survey found that respondents based in Asia-Pacific are more likely to wish to increase the number of suppliers and overall procurement spend, whereas those in the rest of the world on average would prefer to reduce both.

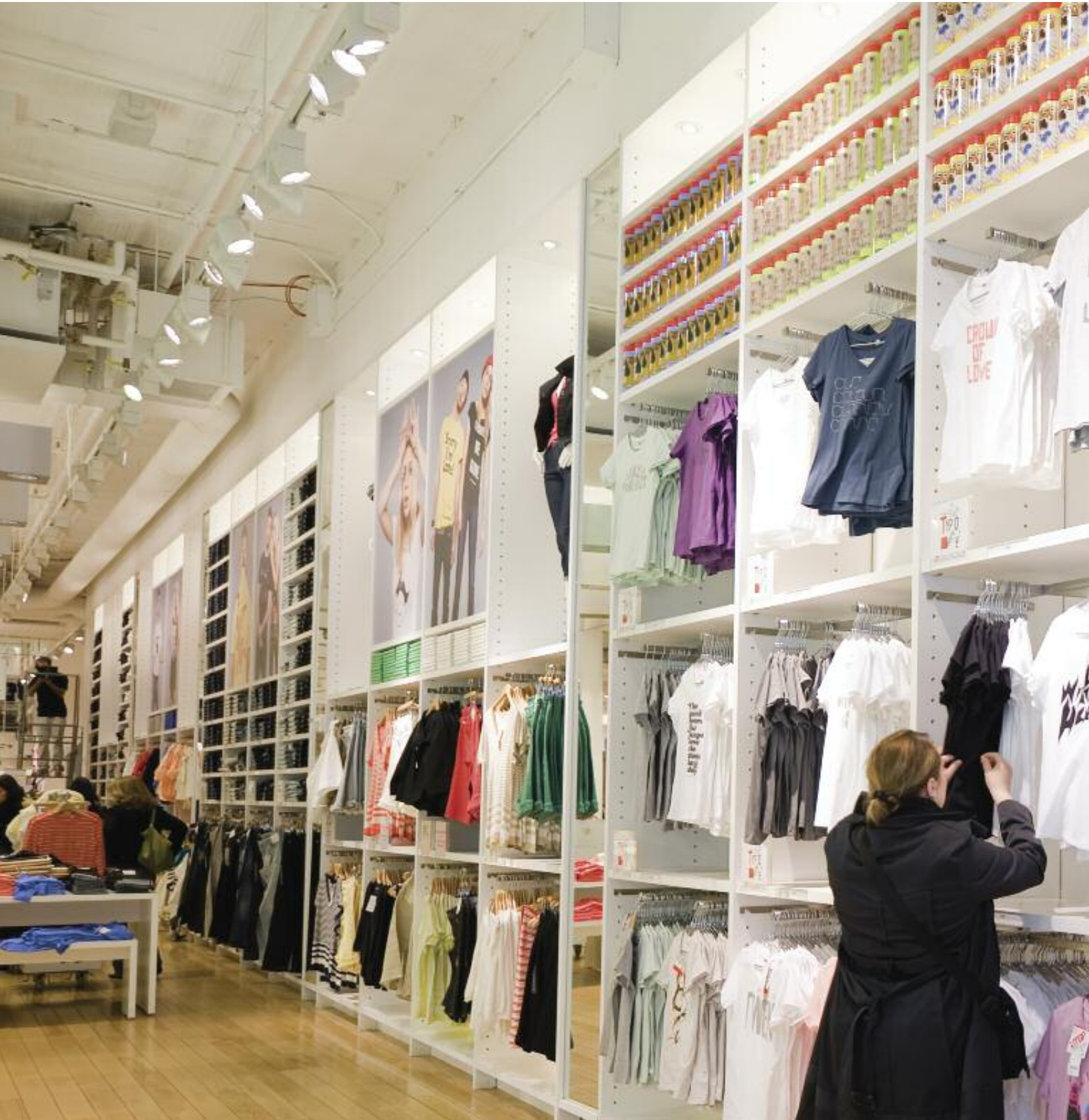
Businesses in expanding, developing economies clearly have different

procurement strategies than those in more mature ones. They might nevertheless benefit from preparation for less rosy times. As Sui Guan Ng, Vice President, Commercial Supplies, Singapore Airlines, reports, procurement is "becoming more and more important as organizations face rising cost scenarios. Because of significant increases in commodity prices, things are getting more and more expensive, and companies have to find more innovative ways to procure their services at cost-effective prices," increasing the need for procurement to contribute to the bottom line.

Strategic initiatives respondents are undertaking or considering







Conclusion

The procurement function is increasingly gaining control over its main raison d'être — the purchase of goods and services for the company. Maverick spending is down; procurement professionals are obtaining authority over more and more day-to-day spending at more and more companies; and centralized functions are becoming best practice.

Even as procurement consolidates authority on its home ground, it faces a variety of broader challenges. Although companies are rapidly investing in information technology to meet the challenges of purchasing in a modern, global marketplace, procurement often lacks the skills required to take full advantage of these tools. Only a minority of businesses are taking advantage of tax-efficient structures. And as scrutiny of companies' environmental and ethical practices increases, there is also a requirement for procurement to understand the implications of corporate sustainability for purchasing and the supply chain.

Meanwhile, efforts to make a bigger contribution to corporate strategy are hampered, often by misunderstanding between the function and the rest of the business. Procurement has much expertise to offer, which can provide substantial financial benefits. Convincing colleagues across the business of this, and aligning not just goals but thinking about where the function can — and cannot — add value, is potentially the biggest challenge in the years ahead.

An inside look: UK Office for Government Procurement — Public sector issues

Although many issues are similar for procurement professionals in the public and private sectors, significant differences exist. Mark Pedlingham, Executive Director of Markets, Suppliers, and Skills at the United Kingdom's Office of Government Commerce (OGC), explains that a larger scale (the British government spends £125 billion annually on procurement), a much broader variety of purchased goods and services, and far greater public visibility, especially of any mistakes, characterize work in his sector.

Our survey also points to another issue: Worldwide, procurement as a function gets less attention and has made less progress toward best practice in the public sector than in the private.

For example:

- Nearly half of public sector respondents say that procurement is only a moderate or low priority in their organizations.
- Over a third report that non-procurement professionals have primary responsibility for day-to-day procurement decisions.
- Public sector respondents are much more likely to complain that procurement in their organizations is overly focused on compliance and processes at the expense of innovation (68 percent against a survey average of 38 percent).

Although these global figures may not reflect the situation in the UK, Pedlingham does agree that “procurement is not quite yet seen in government as a key function. We have some way to go to get to an appropriate level.”

Given the amounts at stake, the UK is instituting the “Transforming Government Procurement” reforms. The broad changes, announced in January 2007, are still in their early stages. The wide variety of initiatives will restructure the OGC and put it in charge of, among other things, the central government's strategic supplier development, collaborative procurement, and procurement policy and standards.

Early results have been promising despite the challenges. Pedlingham notes of collaborative procurement, for example, that “working with one another is something departments do not do naturally. That part of the program has been hard work.” Efforts in this field, which also predate the current initiative, have contributed to the total annual savings of £9.6 billion made through procurement efficiencies.

More important than getting procurement processes right, however, has been helping personnel to develop their potential. Pedlingham explains that the British government's procurement service “had begun to lose value among potential members. We are trying to create a cadre of professionals and be recognized as such.”

One way of doing this is revitalizing the professional organization of government procurement professionals. More broadly, as a key part of initiative, the OGC is conducting Procurement Capability Reviews of every government department. Three departments have so far had such reviews, and “have all found the exercise useful” both in providing a fresh pair of eyes for specific problems and by helping procurement personnel — and their departments — focus on the key issues they are facing.

In considering the early learnings from the initiative, Pedlingham says that “the conversations we've had since January 2007 have enforced the underpinnings which led to this, in particular the question of professionalism and need for a cadre of professionals.” In this at least, private sector professionals would certainly understand the issues involved.

KPMG final thoughts: Achieving a world-class procurement function starts with planning

Many organizations begin reorganizing and improving their procurement after they realize that they are not achieving maximum cost savings, and that their business units are not pleased with the procurement function. However, they reorganize without a clear idea of what is wrong with the function or how they want it to work once it's been reorganized. Consequently this realignment doesn't achieve its goals, and procurement continues to be the corporate underachiever.

Any successful procurement function must be structured so that it manages and uses working capital in the most efficient manner possible.

This successful move to more efficient management of this capital begins at the strategic and planning level. As stated, an effective procurement strategy must be aligned with corporate strategy, and there must be buy in to this at the executive level. The details of that strategy will be unique to the organization, but everyone must be on board. One of the biggest mistakes procurement can make is to present a fait accompli. A successful reorganization of procurement will include an open dialogue with business managers and clear explanations of what will happen and what it means.

Organizational buy-in remains a prime roadblock

In our experience, getting this organizational structure and buy in right is the single most difficult problem in

procurement restructuring. Too many organizations fail to do the upfront work required to properly understand how the old and new will interact when they institute major changes. This is one reason KPMG's procurement specialists often recommend incremental change by testing a new procurement structure with one product or division. Learn from that and then expand. Too many significant cost savings in an efficient procurement model can be lost through hurried or inadequate implementation.

Getting it right also requires effective metrics to be in place. If an organization does not have the means to determine if it is achieving its goals, it will lack the ability to adjust and improve its processes. Furthermore, when procurement prepares to alter its approach, it must ask itself if it has the skills to implement a new vision. Do not expect a team trained in negotiating with local suppliers to suddenly develop strategies for a global sourcing plan. If the skills aren't there, they must be brought in for procurement's new role to be a success.

IT, taxation, and sustainability all demand upfront planning

This truth extends to IT and taxation issues, as well. While organizations must remember that better IT is only an enabler and not an end in itself, they must also remember it will be neither without people who have the analytical skills to use the technology and interpret the data. The strategy must be thought through, and the structures and people

in place; then get the automation implemented effectively. As highlighted, this is another downstream result of good upfront planning.

When looking at decisions around the location of any procurement structure, this kind of planning must also include the corporate tax department. This may mean reaching across traditional barriers but it must be done to maximize savings.

And lastly, while there may be many unanswered questions around sustainable business practices, no smart organization can afford to delay addressing this issue.

Two basic keys to world-class procurement

The procurement organizations we at KPMG tend to admire do two things very well. They plan meticulously before taking any action, and then they continually adapt and tweak their processes once they have taken action.

These organizations are constantly looking for new places to add value and seek to discover new opportunities. Their culture is one of curiosity and audacity: it learns and is not afraid to adapt. In order to draw the correct conclusions that drive this constant adaptation, it's important to note that these procurement functions are also highly metric-driven. In our experience, success in all other areas of the procurement function derives from these two constants of good planning and a readiness to evolve.

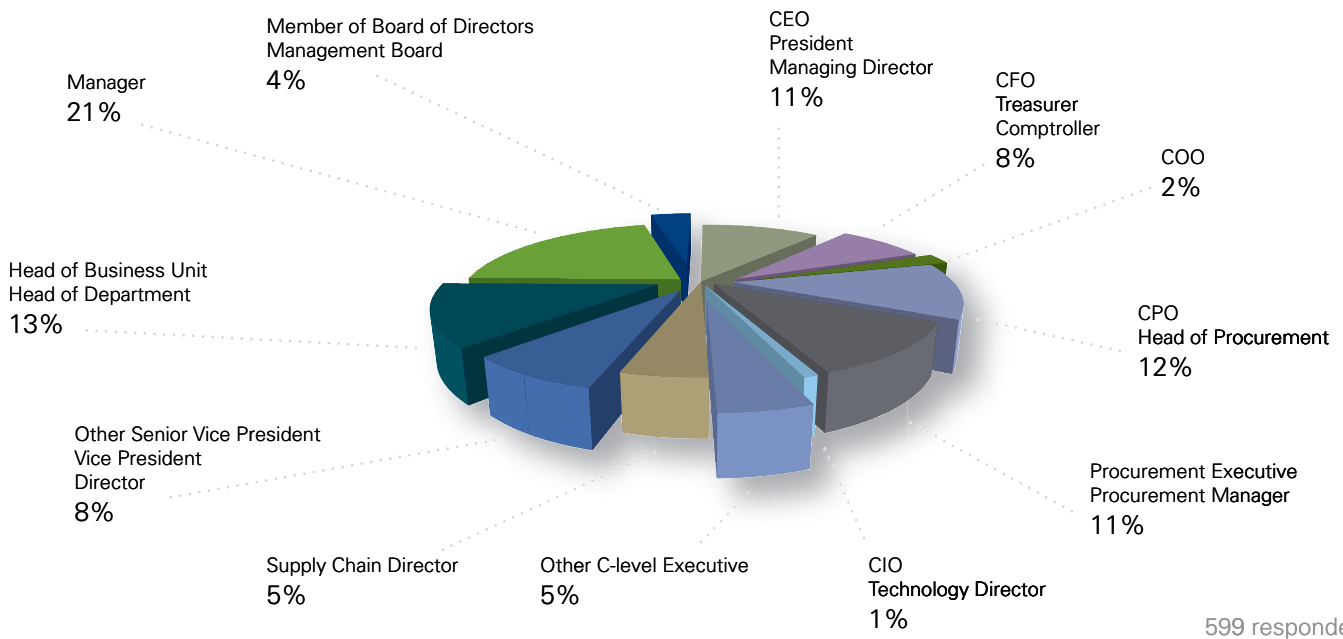
Written by KPMG

Appendix. Survey results

This research was conducted by the Economist Intelligence Unit in 2007 and 2008. The senior executives who responded to the survey were drawn from a cross-section of industries and included 322 procurement decision makers. What follows is a compilation of the survey results as well as detail about the respondents and their organizations.

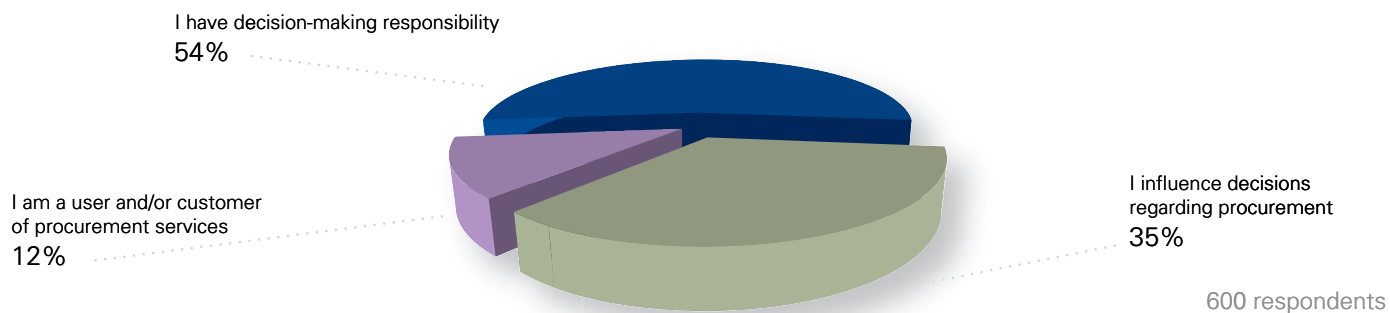


1. Which best describes your role at your organization?

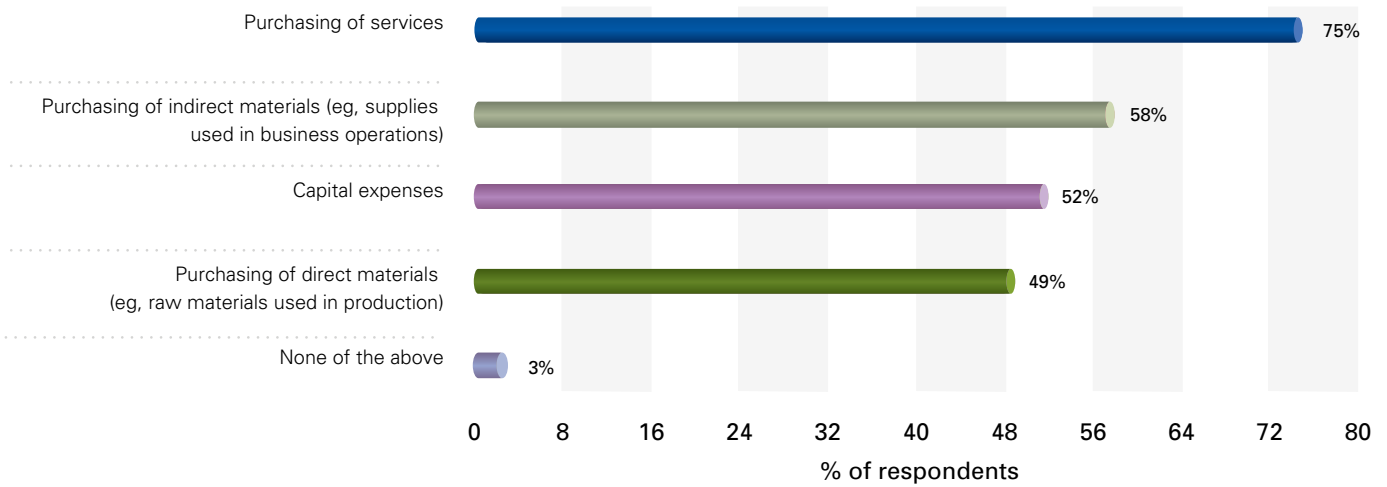




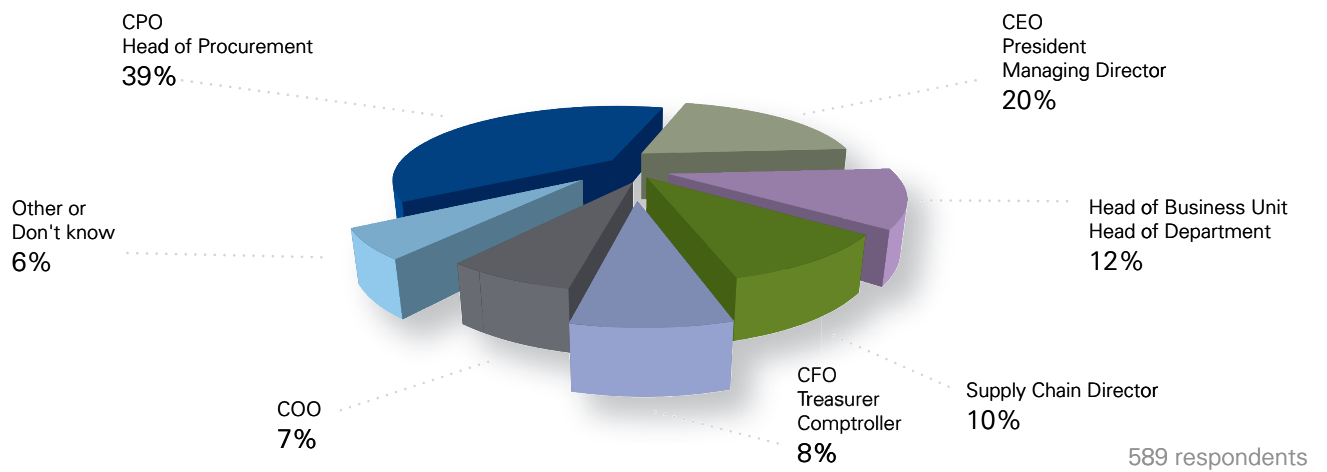
2. Which best describes your role in procurement?



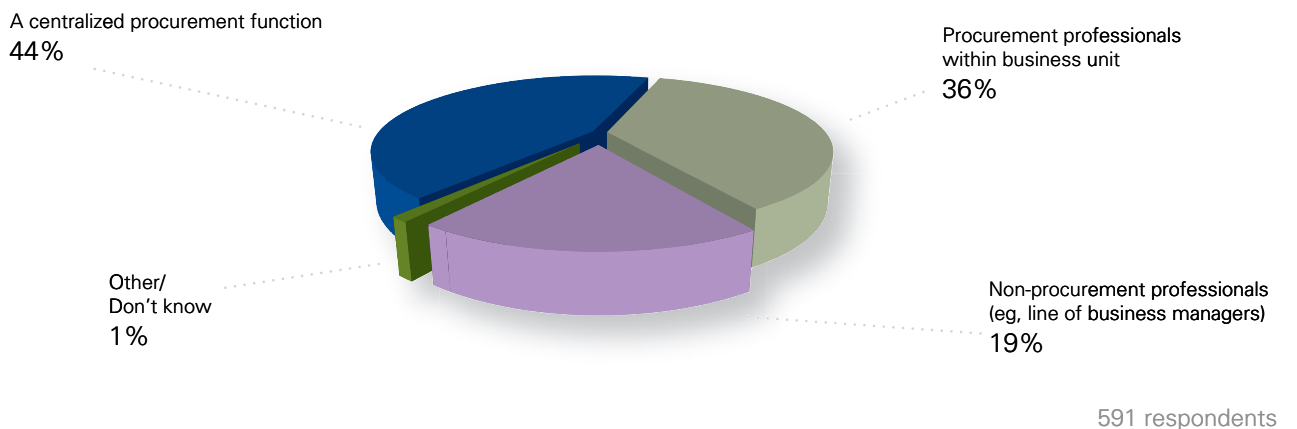
3. In which of the following areas do you have an influence on procurement decisions? Select all that apply.



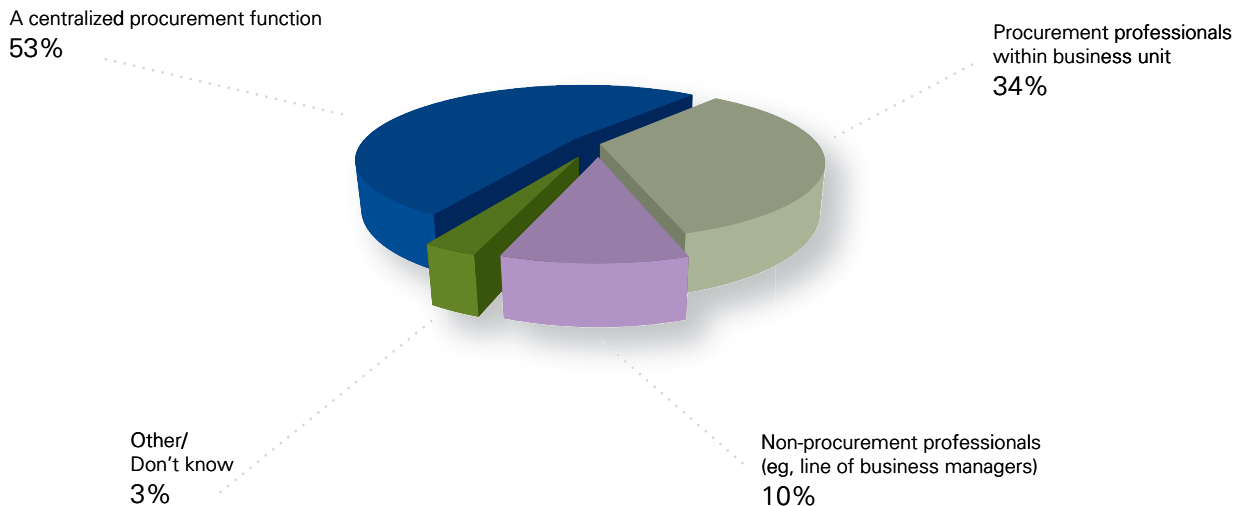
4. Who is primarily responsible for setting procurement strategy in your organization?



5a. Which of the following is primarily responsible for day-to-day decisions on procurement in your company today?

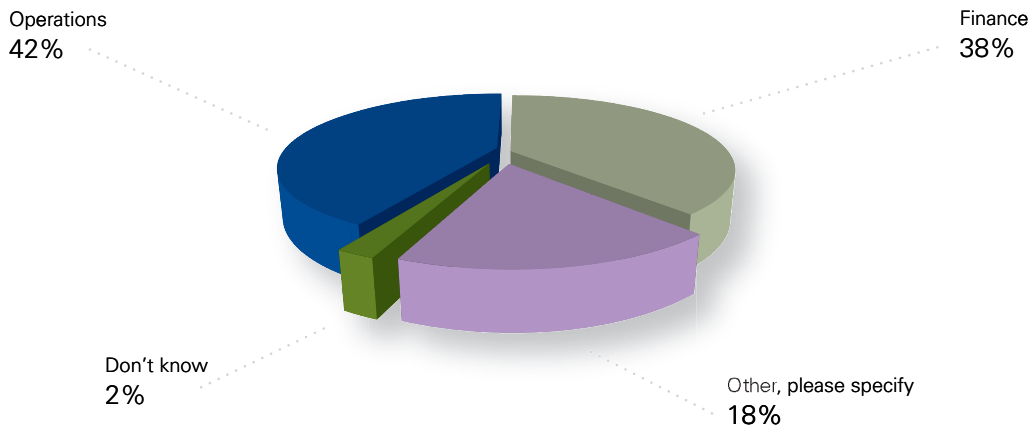


5b. Who do you think will be responsible in three years' time?



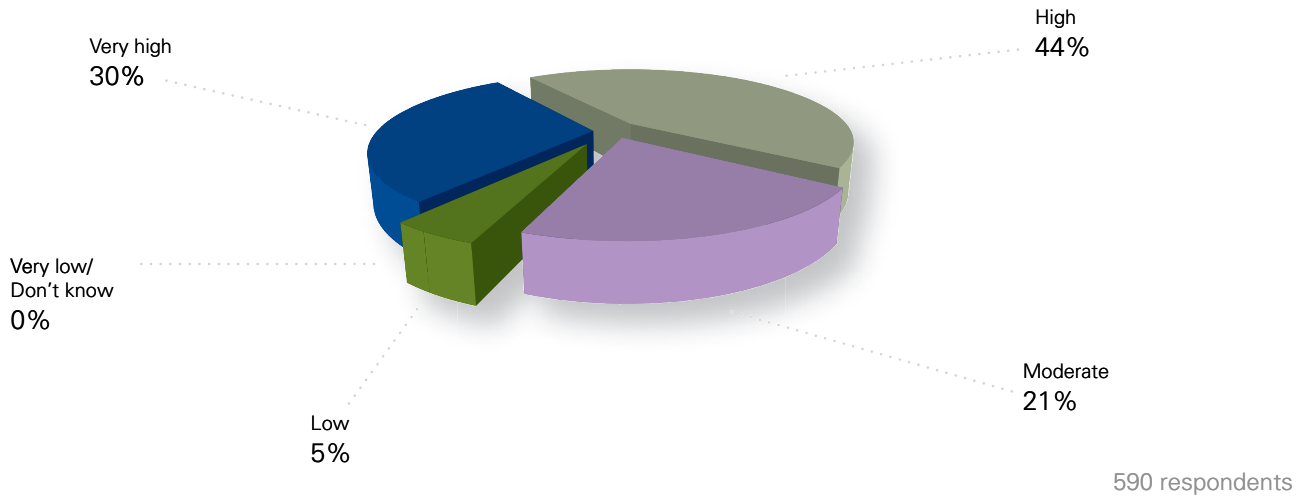
592 respondents

6. To whom does the procurement function report at your organization?

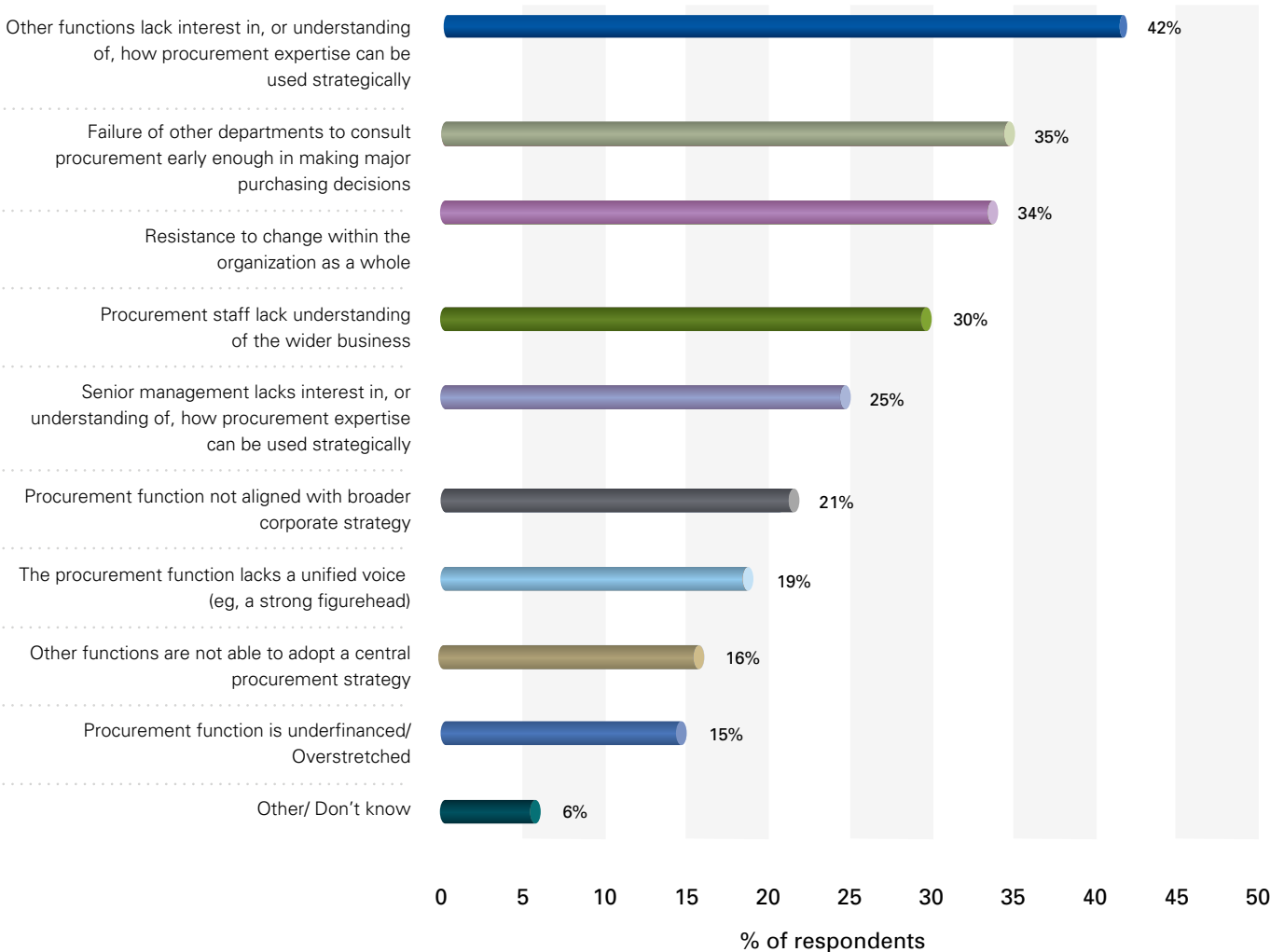


582 respondents

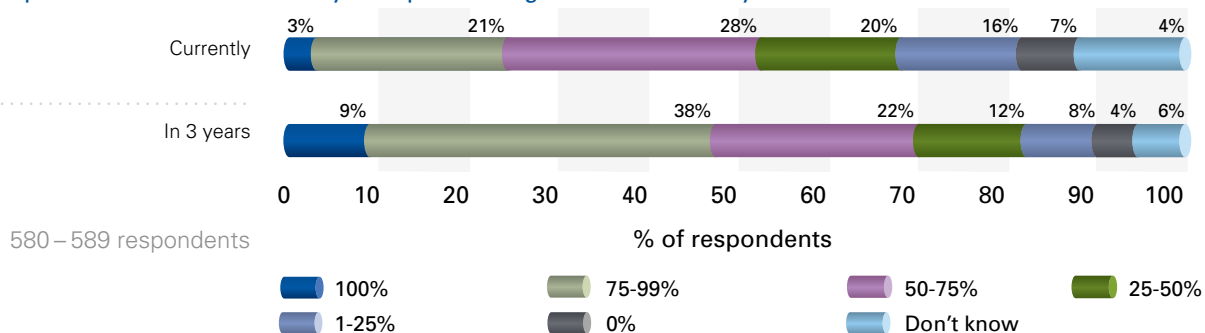
7. How high a priority are procurement issues for your organization?



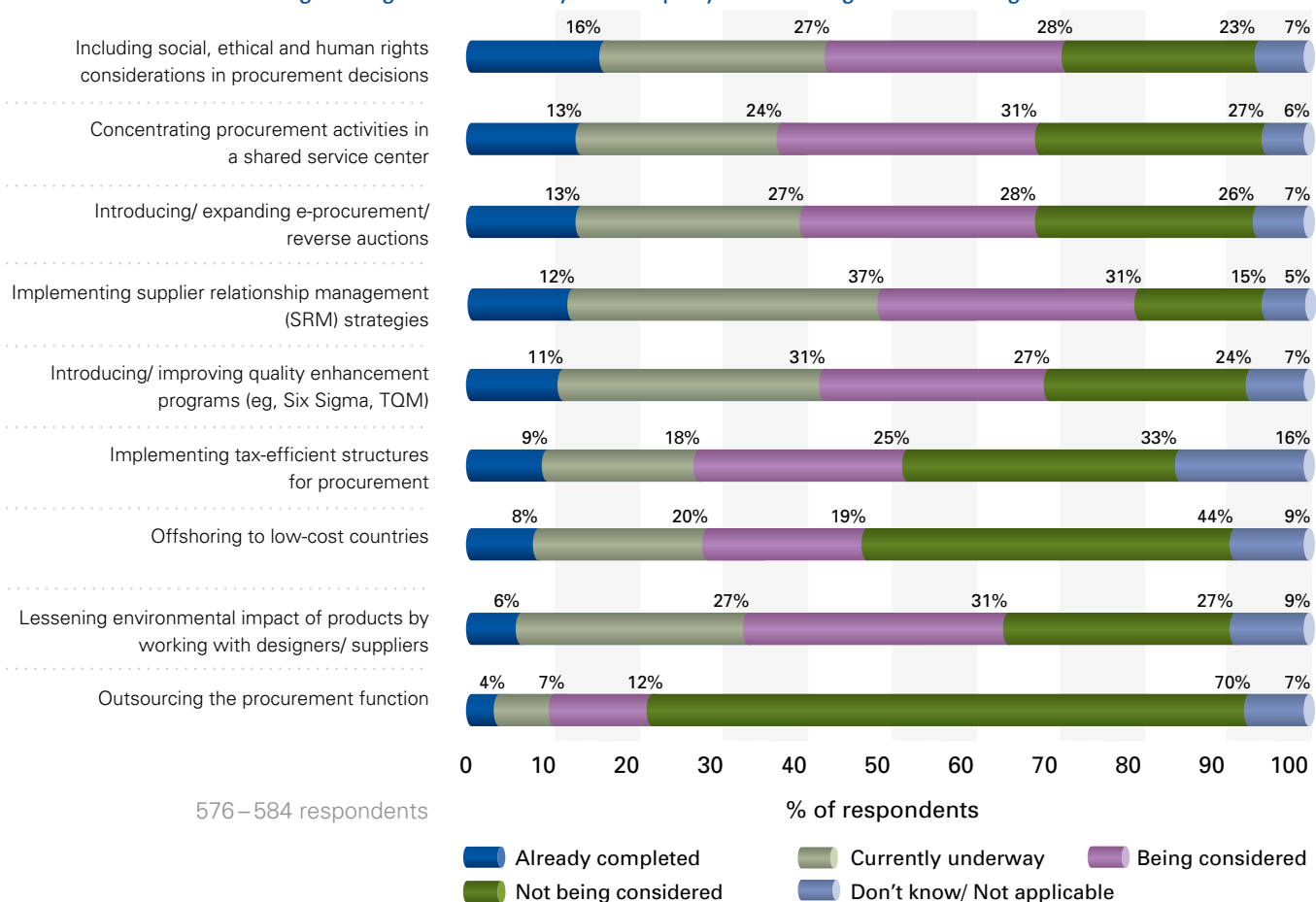
8. Which are the biggest barriers to a greater strategic impact for procurement at your organization?



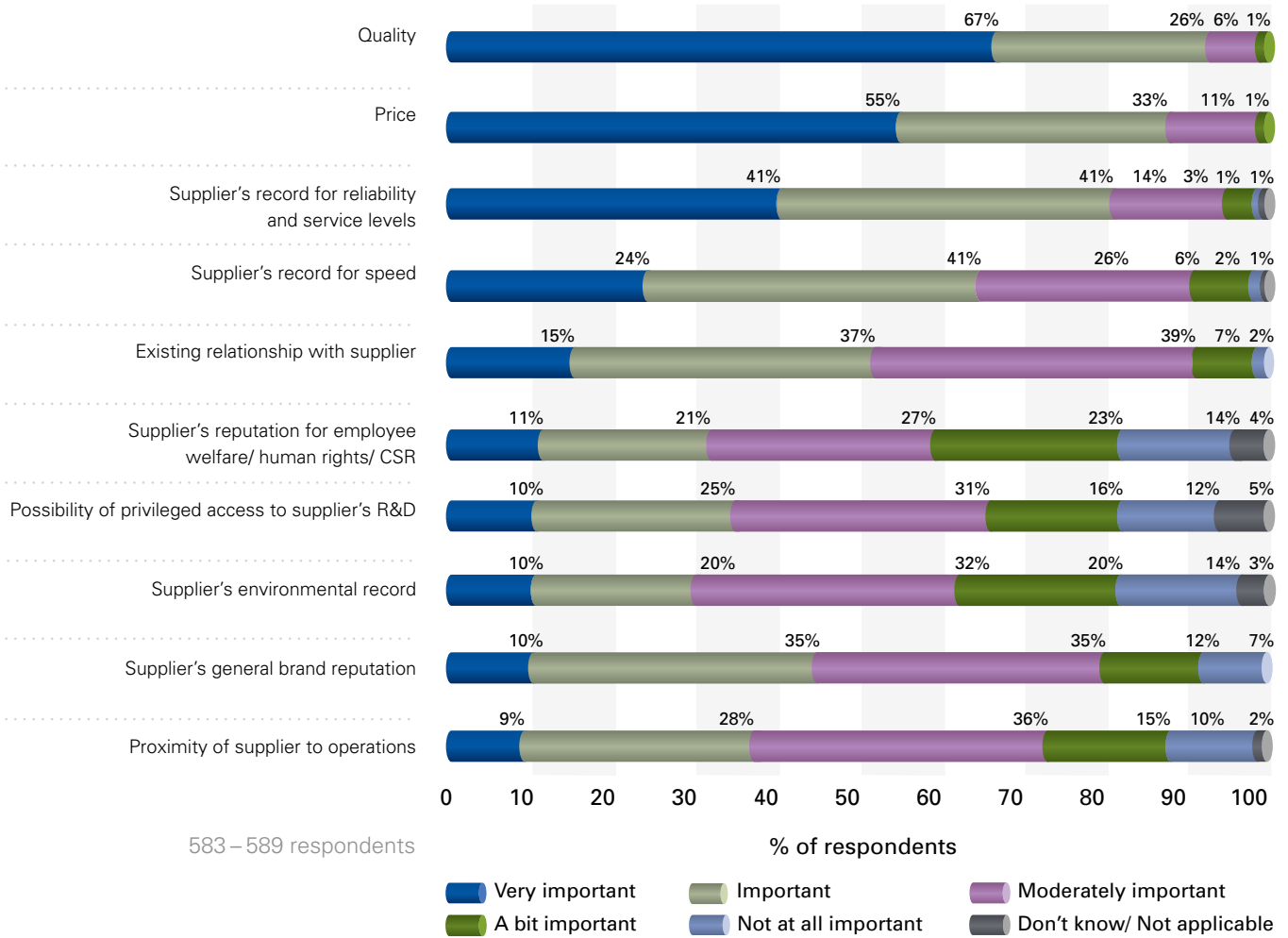
9. What percentage of total procurement spend (direct and indirect) at your organization is negotiated or contracted by procurement professionals and what do you expect this figure to be in three years time?



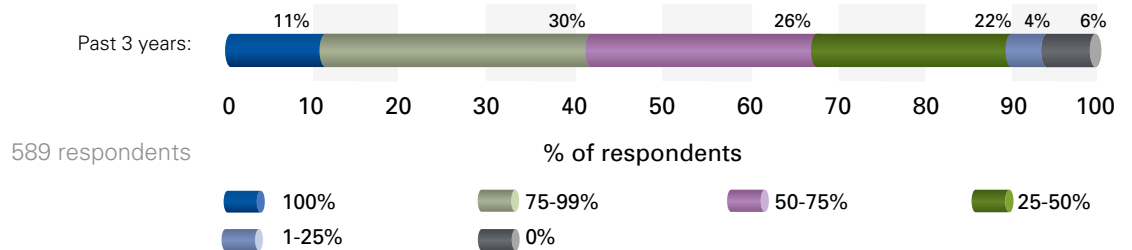
10. Which of the following strategic initiatives is your company undertaking or considering?



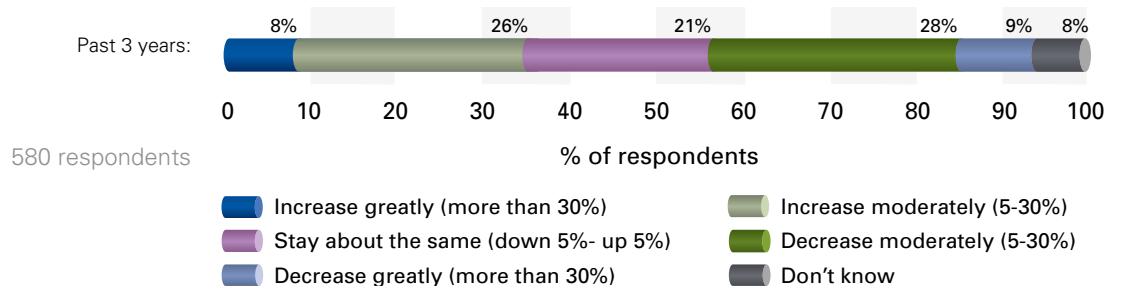
11. How important are each of the following to your company when selecting a supplier for a major contract?



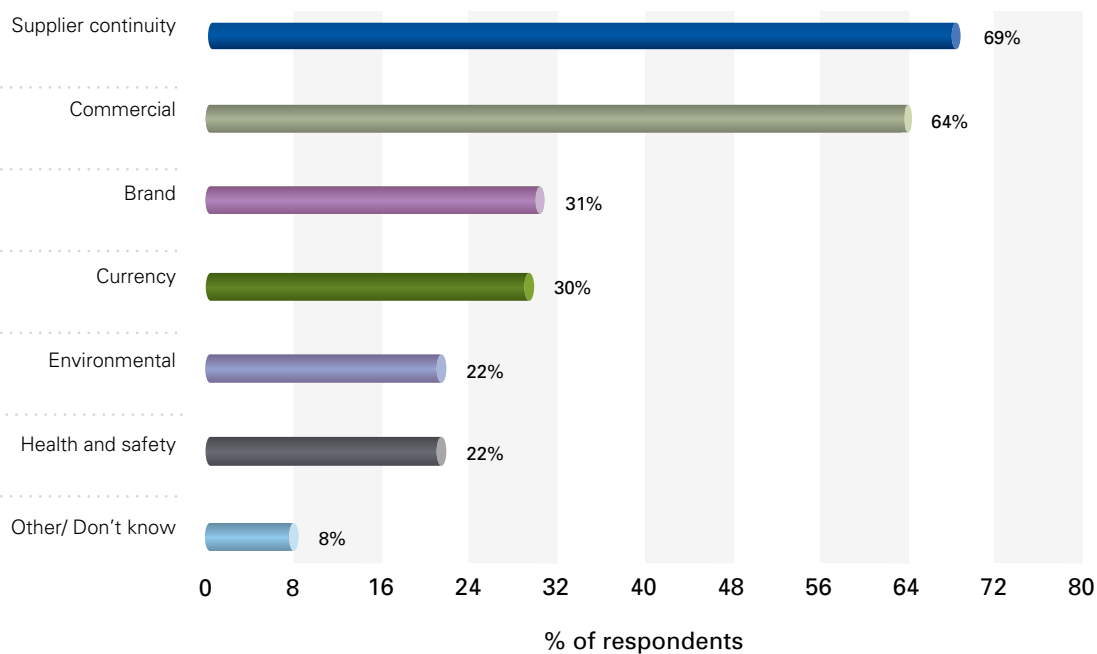
12a. Over the past three years, how has the number of suppliers to your organization changed?



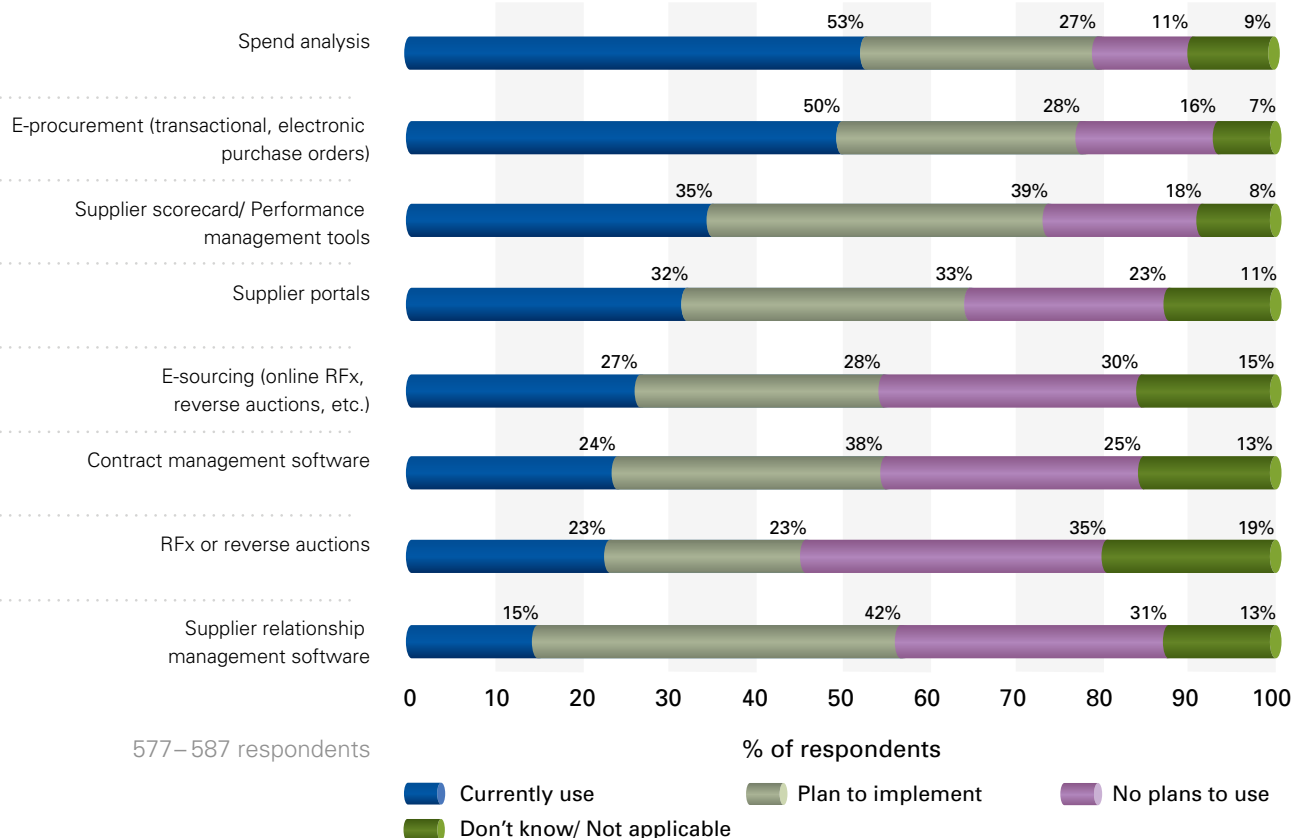
12b. What change do you expect over the next three years?



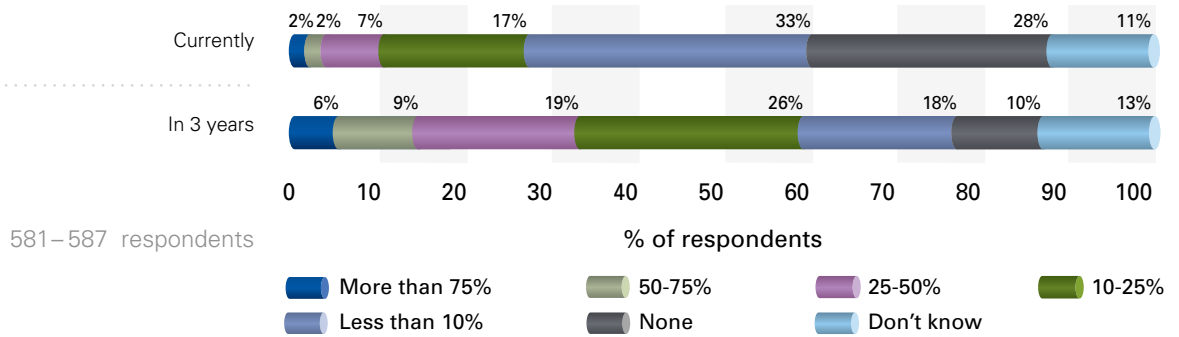
13. What are the most important kinds of supplier risk to your organization?



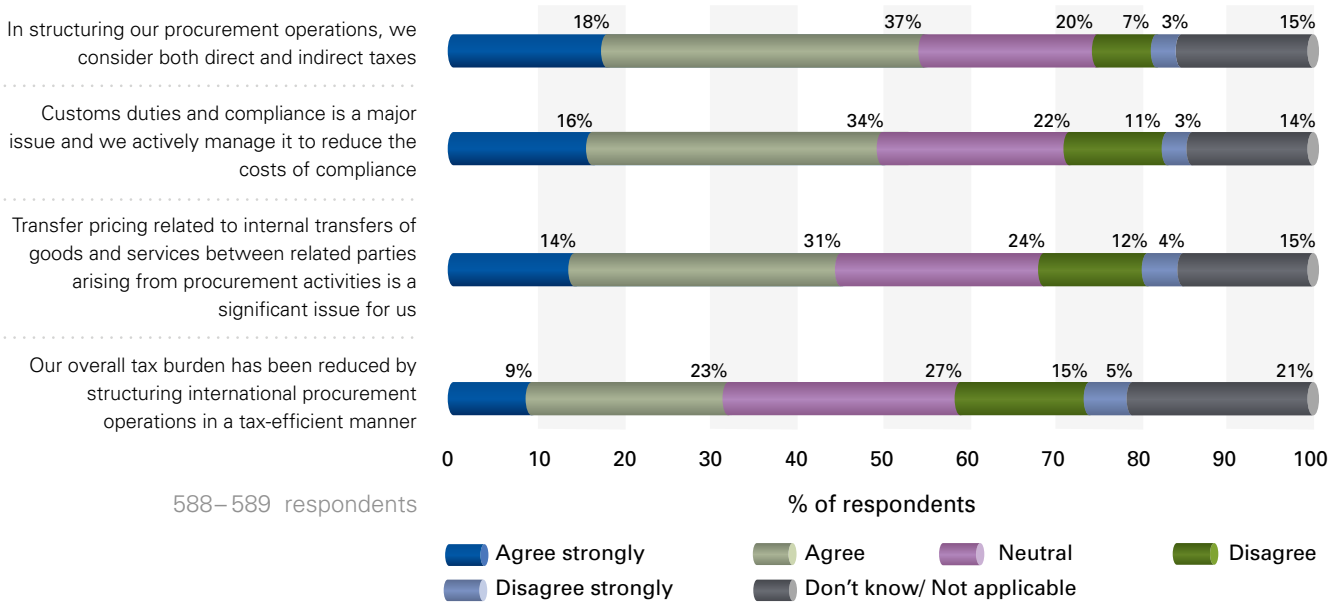
14. Which of the following IT tools does your organization use, and which does it expect to implement in the near future?



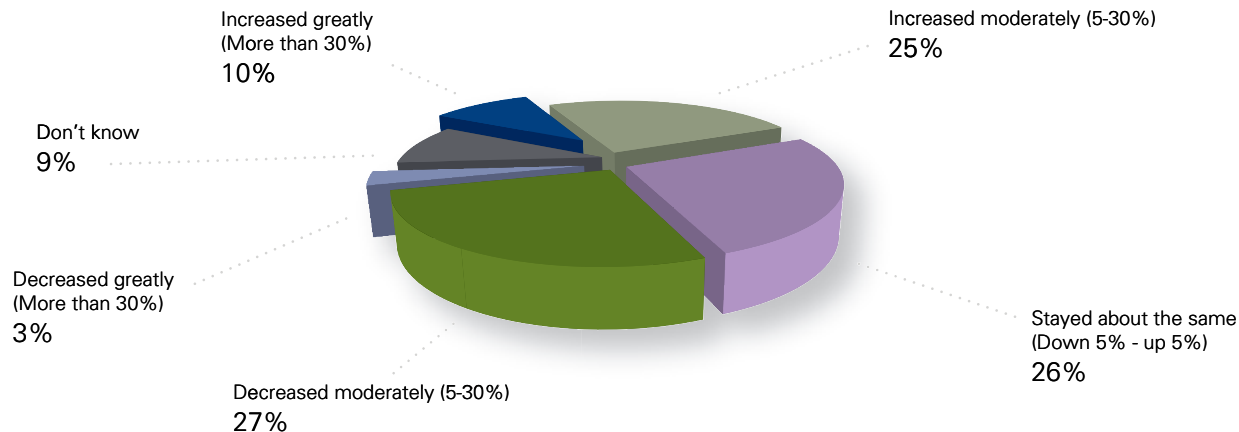
15. What percentage of your company’s procurement spend is channeled through e-sourcing or e-procurement (e-RFx, e-auctions)? What do you expect it will be in three years’ time?



16. When considering international procurement operations, how strongly do you agree or disagree with the following tax-related statements?

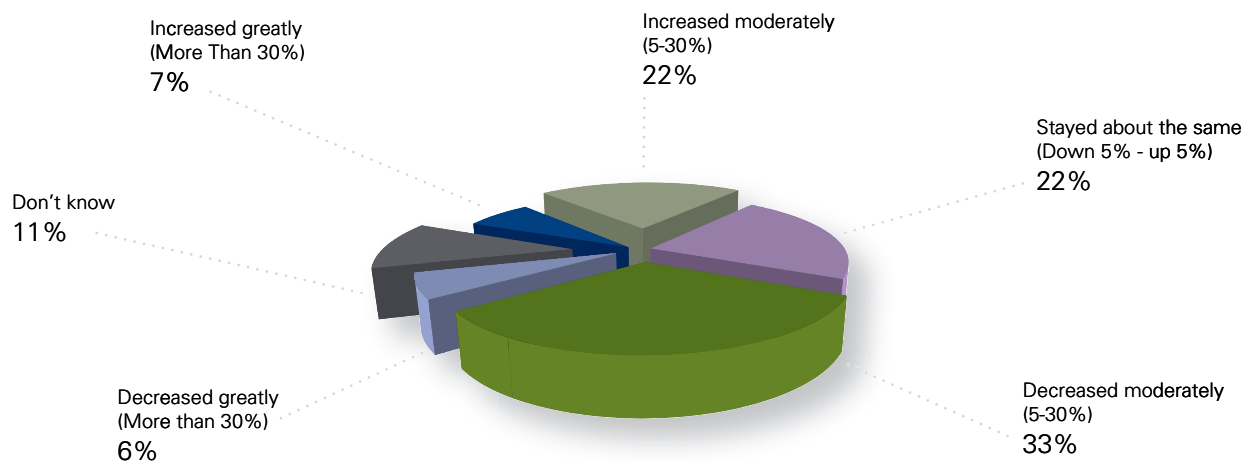


17a. How much has the procurement function changed your organization's procurement cost base in each of the last three years, on average?



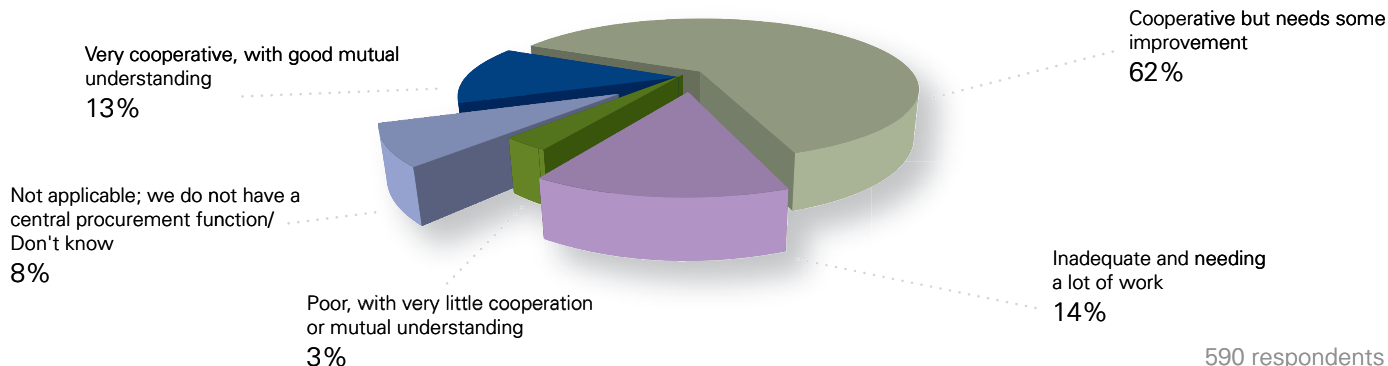
587 respondents

17b. What goal does it have for each of the next three years, on average?



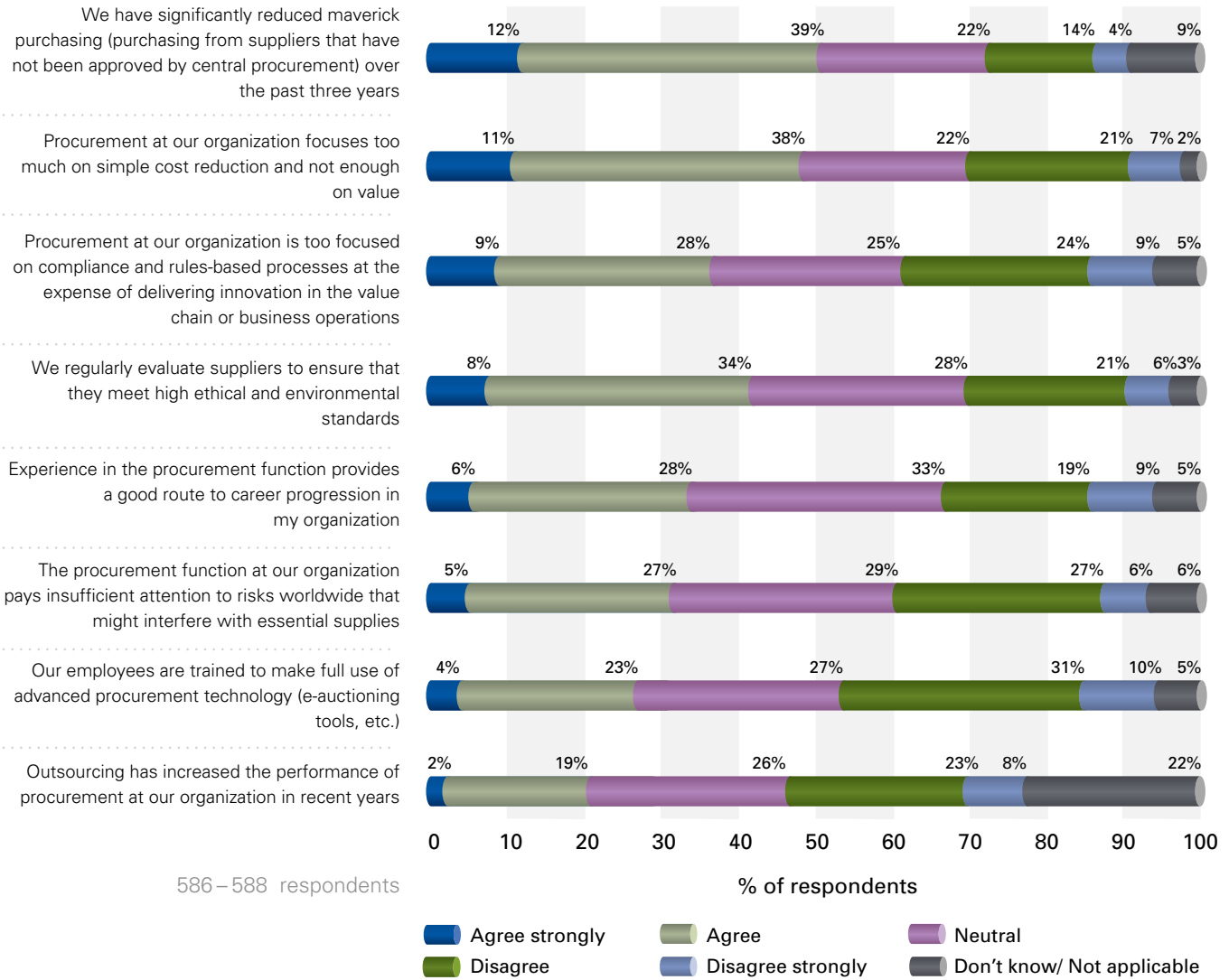
582 respondents

18. How would you describe the relationship of your organization's central procurement function with its internal customers?

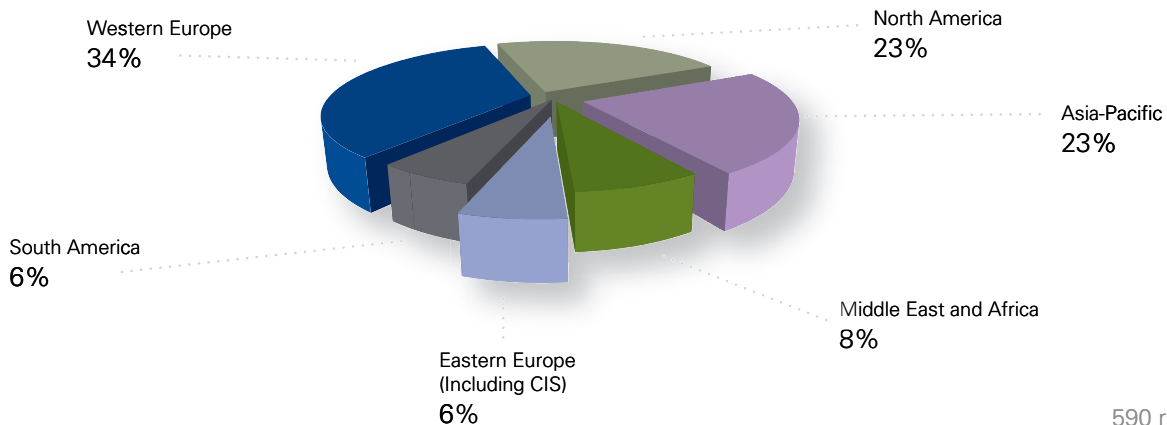


590 respondents

19. How strongly do you agree or disagree with each of the following statements?

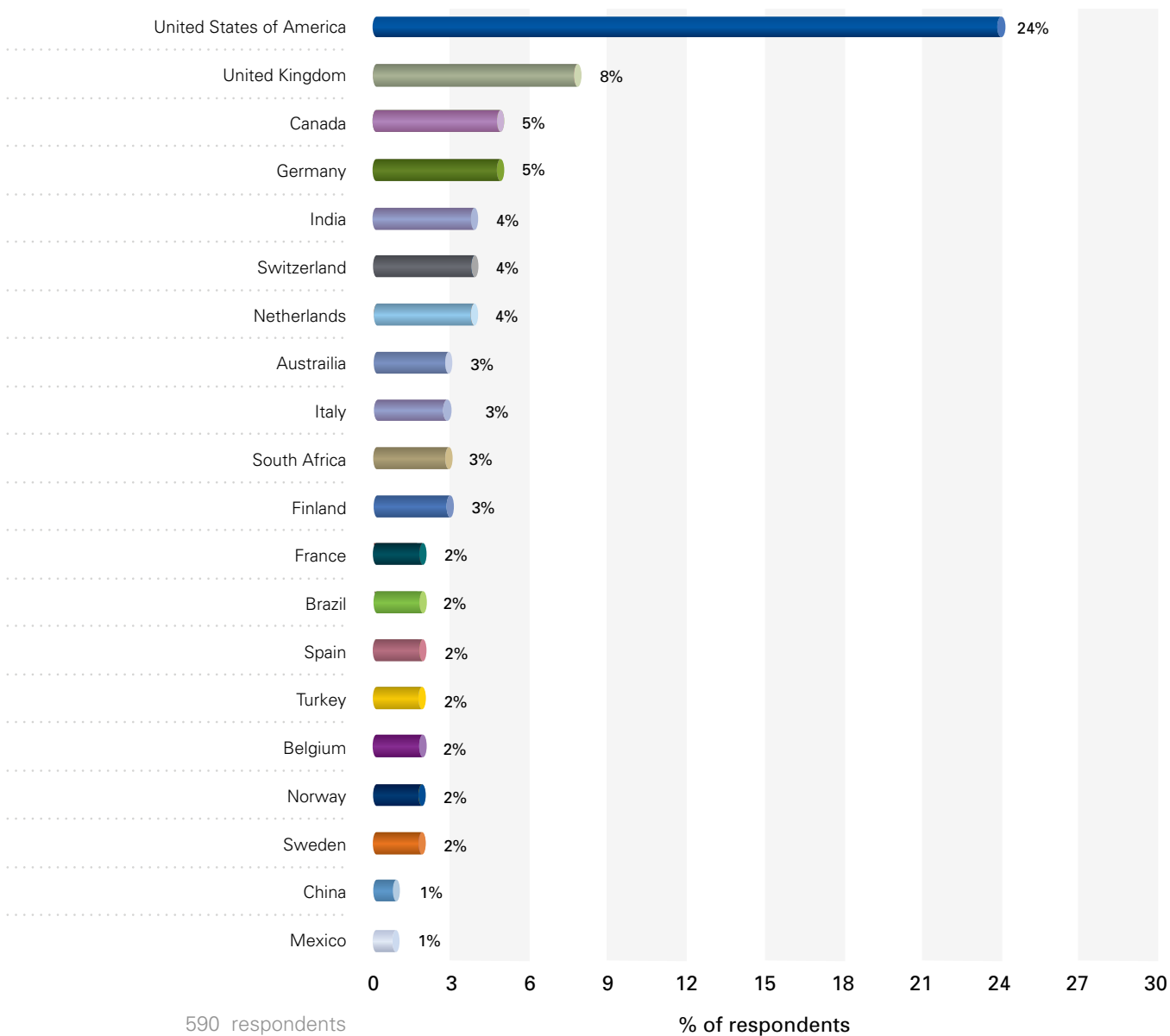


20. In which region are you personally based?

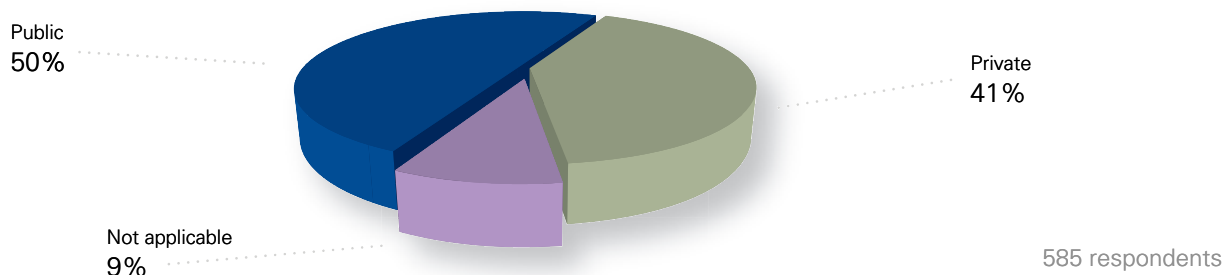


21. In which country is your organization headquartered?

Top 20 countries

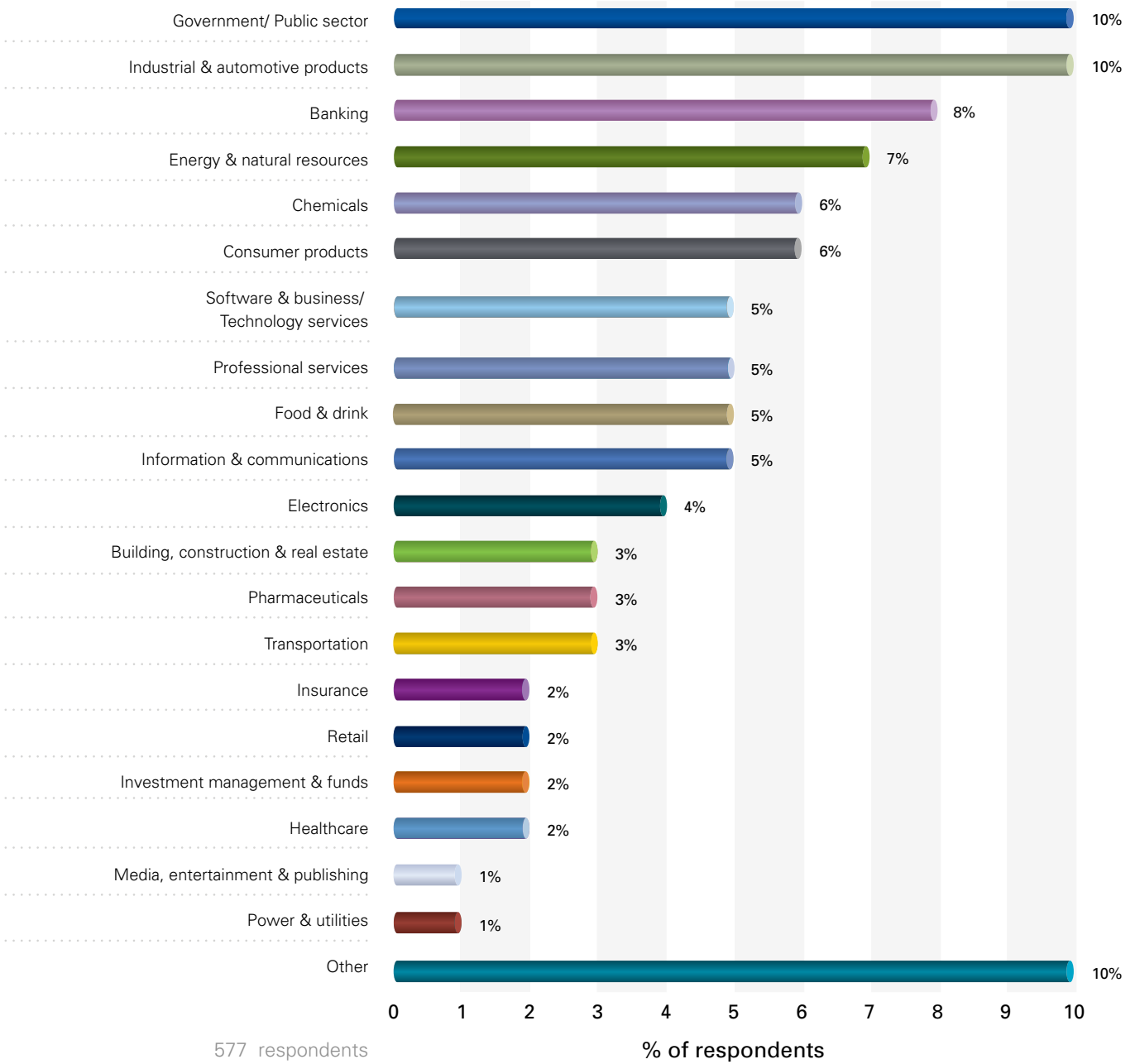


22. Is your organization publicly listed or privately owned?

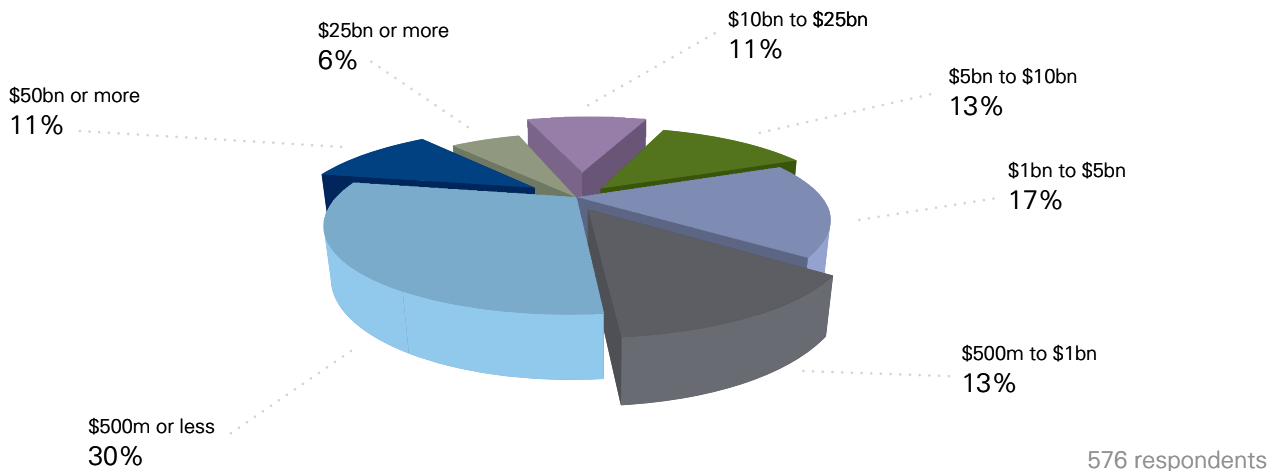


23. What is your industry?

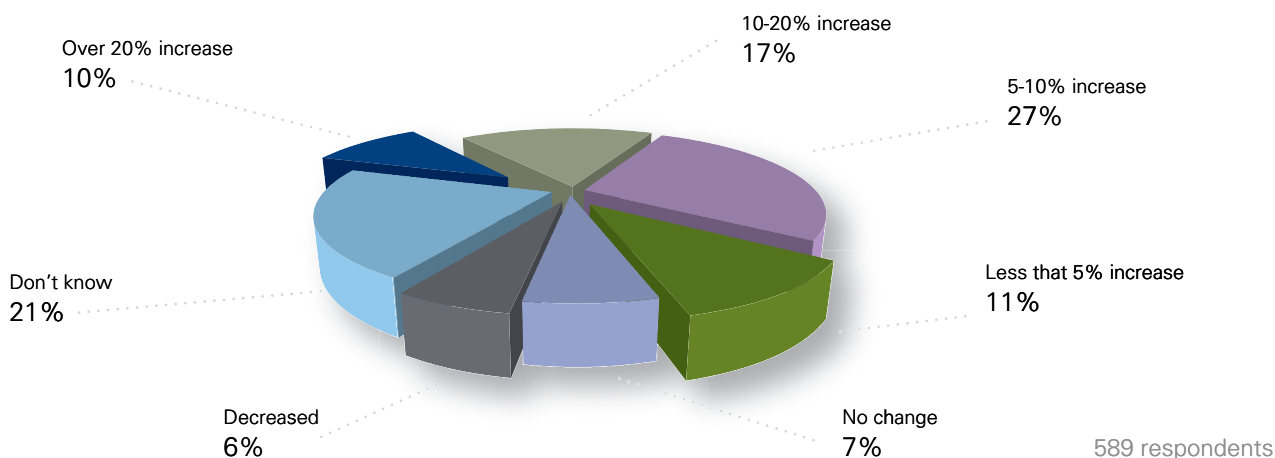
Industries



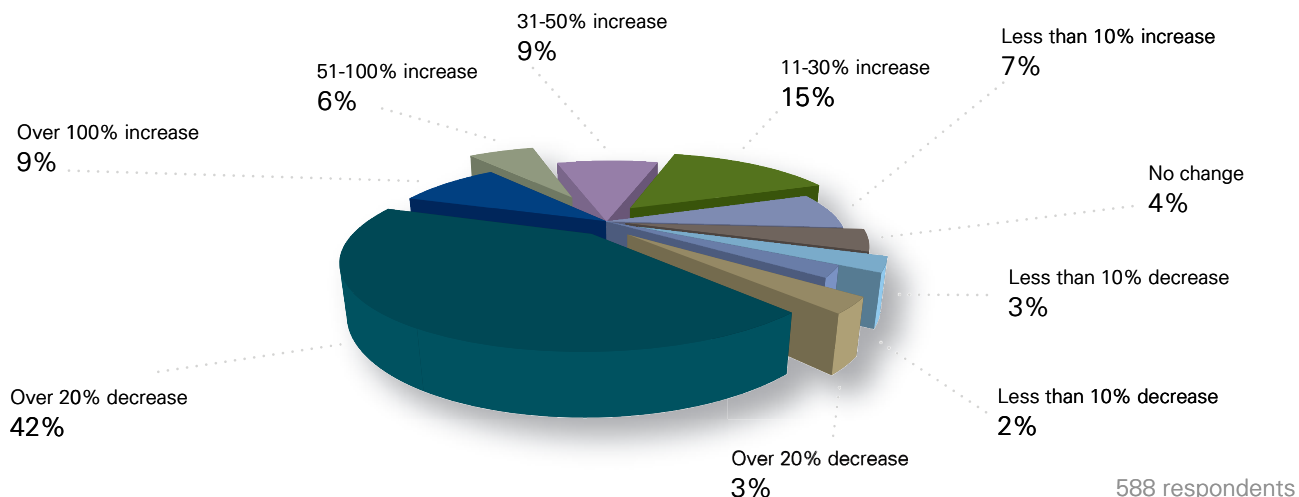
24. What are your organization's global revenues in US dollars?



25. How has your organization's EBITDA changed each year, on average, over the past three years?



26. How has your organization's share price changed over the past three years?







Thanks to everyone who participated in making this research report possible, but special thanks go to the key contributors of this publication whose insight, experience, perspectives and passion for this research effort made it happen:

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About the design

Procurement has become a search for goods that extends around the globe. For this reason, we have chosen visual imagery for this research report that highlights the concept of a global marketplace, as a metaphor for the new role of procurement.

We have selected images from farmer markets to financial markets. Procurement now reaches all areas of commerce and involves nearly all aspects of the global economy. At its core, it has become nothing less than the foundation of the capitalist system. The imagery we employ here is selected to relate to the global reach and power of the procurement industry.

Written by KPMG

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